FINANCIAL HISTORY

The magazine of the Museum of American Finance

Founder Makes Final Visionary Gift to Museum

Boardroom Battles and the Rise of Shareholder Activism

Financial Innovation: Catastrophe Bonds

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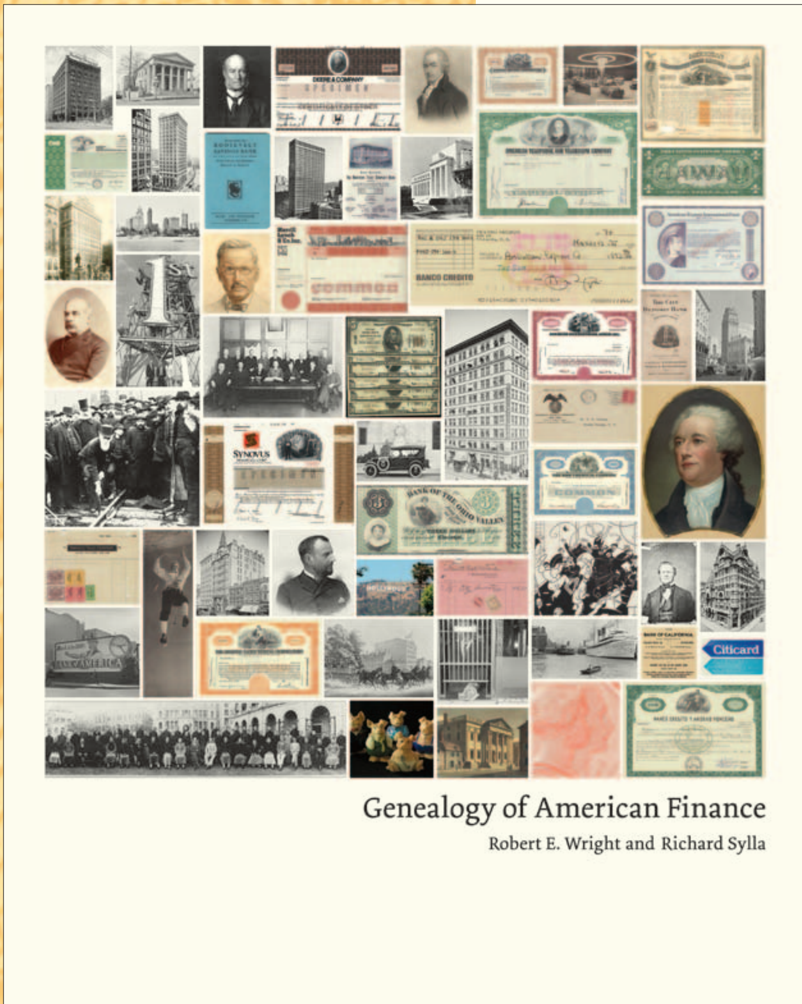

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www.moaf.org/newbook

Genealogy of American Finance

By Robert E. Wright and Richard Sylla

Foreword by Charles M. Royce

> "*Genealogy of American Finance* is a treasure trove of information on American banking and its history, in an unusual—and unusually useful—format."
>
> —*John Steele Gordon, author of* Empire of Wealth

An immersive history of 50 major American banks and their transformation of the nation into a leading world power.

In this gorgeously illustrated hardcover book—published by the Museum of American Finance and Columbia Business School Publishing—readers learn how 50 financial corporations came to dominate the US banking system, shaping the nation's political, social and economic growth along the way. A story that spans more than two centuries of war, crisis and exciting promise, this account reminds readers that American banking was never a fixed enterprise but has evolved in tandem with the fits and starts of the country. A key text for navigating the complex terrain of American finance, this volume draws a fascinating family tree for projecting the future of a nation.

MUSEUM OF AMERICAN FINANCE

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FINANCIAL HISTORY

THE MAGAZINE OF THE MUSEUM OF AMERICAN FINANCE

in association with the Smithsonian Institution

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Kristin Aguilera
Editor

IN THIS ISSUE FEATURES

IN THIS ISSUE DEPARTMENTS

ON THE COVER

Wall Street veteran and Museum of American Finance founder John E. Herzog — pictured here with the Board of Trustees — gives a final legacy gift to the Museum. See article, page 5.

Alan Barnett

The Past, Present and Future of the Museum

Message to Members

David J. Cowen | President and CEO

Today I write to you about the past, the present and the future of the Museum. As you can see from the photograph below, John Herzog has made a final major gift to the institution he founded some three decades ago. John, the staff and the Board can take pride in the enormous progress the Museum has made since then. With this final gift, John is passing the torch symbolically and financially to the next generation of supporters.

As we begin to think about the next chapter in the Museum's life, Chairman Richard Sylla has created a "Committee of the Future" comprised of key members of our Board and staff. While we all enjoy the architectural beauty and historical relevance of our home at 48 Wall Street, we realize that we may need to vacate this space in the near future, as our lease will expire in 2021.

While five years may seem like a long lead time, in the museum world it is not. The Committee will be working on finding a more permanent home, while at the same time creating an overall plan and blueprint for what the Museum could be. Our goal is to ensure that after engaging with the exhibits, visitors leave with an understanding of the importance of finance-led growth to the American economy that is created by our free enterprise system. Unlike an art museum, where the works speak for themselves, we must bring this message to life through our interpretation of the story. We believe the way to explain this is through three major components (the three Ps): Public, Private and Personal Finance.

The Public Finance component will explain how the nation funded incredible advancements — from the Louisiana Purchase to the space program — and will also explore and bring to life the current amalgam of debt in the country. The Private Finance track will explain how companies are funded through debt and equity, the history of exchanges and how that has led to growth, while at the same time highlighting the various areas of free enterprise including real estate, life insurance and entrepreneurship. Lastly, the Personal Finance section will be dedicated to personal financial literacy — savings, budgeting, mortgages, etc. Finance is an important part of our lives but, sadly, as a nation we are financially illiterate.

In addition to the core exhibits, we envision a high tech and engaging currency exhibit, timely temporary exhibits, expanded programming and interactive teaching capability to reach classrooms throughout the nation. I hope you can see why the Committee is excited.

Of course, this new vision will take time and money. John Herzog has given us a head start, and now it is up to all of us to take the Museum to the next level. The Board, staff and I are looking forward to that challenge. $

Alan Barnett

John Herzog hands a check representing his final major gift to the Museum to Chairman Richard Sylla and President David Cowen at an event on May 17.

MAY 7 1825

The first known buying frenzy for an American IPO is reported, as the Bank of Southwark goes public on the Philadelphia Stock Exchange.

MAY 9 1901

As competing bull and bear factions try to corner the market in Northern Pacific Railway stock, the shares hit $1,000 — up from $96 five weeks earlier.

Museum Founder John Herzog Makes Final Visionary Gift to Institution

By Kristin Aguilera

Wall Street veteran John E. Herzog announced a final $5 million gift to the Museum of American Finance, the institution he founded more than 25 years ago, at an event held in his honor on May 17. Herzog established the Museum in response to the Crash of '87 and has been the institution's largest donor ever since.

Herzog's most recent gift, which he communicated to the Museum's Board of Trustees on his 80th birthday, represents the sum he had earmarked for the institution in his will. His gift echoes the advice of Andrew Carnegie, who advocated philanthropy within one's lifetime.

"This final gift is a display of my confidence in the ability of the Museum's leadership to successfully carry it into the future and sustain it as a permanent institution," said Herzog.

In 2010, Herzog stepped down as Chairman of the Board and became Trustee *Emeritus*, making way for new leadership and a new class of Trustees poised to usher the institution into the future. Since then, the Museum has added 28 new Trustees and has greatly expanded its individual and corporate donor bases.

"We are extraordinarily grateful to John for his support of the Museum over nearly three decades," said Chairman Richard Sylla. "However, like any non-profit institution, the Museum's future depends on a broad commitment from a variety of donors, members and constituents."

In addition to increasing the size and stature of its Board, the Museum has also engaged new audiences through enhancements to its educational and programmatic offerings. Many of its educational initiatives now focus on promoting personal financial literacy, which is lacking in both children and adults across nearly every segment of the population.

The Museum is always seeking increased participation from financial firms — both as donors and as programmatic partners — while serving as a neutral public forum for addressing topical financial issues and events. In the past two years, the Museum has presented more than 50 programs on a wide variety of current — and often forward-looking — topics, ranging from Bitcoin to IPOs to electronic trading.

The May 17 reception marked a symbolic moment in the Museum's history, as its founder entrusted responsibility for the institution to the next generation of leaders and supporters. $

John Herzog speaks at the May 17 event held in his honor.

Trustees John Davidson and David Shuler.

Former Trustees in attendance included (clockwise from back left): Ken Winans, Tom Levis, Bill Pinzler, Bill Behrens, Michael Lipper, Jason Zweig and Timothy Schantz.

Alan Barnett

Barbara Brown, Guy Taylor, Sidney Mobell and Gabriel Suprise.

MAY 10 1965 In New Bedford, MA, a young Warren Buffett takes control of a decrepit textile company called Berkshire Hathaway Inc.

MAY 14 1997 Amazon.com, Inc. goes public on the Nasdaq, offering three million shares at an initial price of $28 per share.

MAY 16 1949 The Tokyo Stock Exchange, originally founded in 1878, reopens for business following World War II.

MUSEUM OF AMERICAN FINANCE BENEFACTORS ($1,000 AND ABOVE)

The Museum is most grateful for the financial support of these major donors in the past year to help advance our commitment to preserving, exhibiting and teaching the power and value of American finance.

- Abner Herrman & Brock, LLC
- John Adams
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- The American-Scottish Foundation
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- Van Eck Global
- Vested
- Paul Volcker
- Voya Financial
- Taylor Wagenseil
- Wells Fargo & Company
- William Penn Foundation
- Anthony Yoseloff

► For information about the Museum's benefactor program, please contact Mindy S. Ross at 646-833-2755 or mross@moaf.org.

MAY 26 1896 Charles Dow creates the Dow Jones Industrial Average with 12 component companies.

JUN 1 1720 One of the greatest speculative bubbles in history nears its peak, as South Sea Company stock shoots from 610 to 870 on June 1–2. Within weeks, the shares drop below 150.

Volunteer Spotlight: Andrew Schmidt

Volunteer docent Andrew Schmidt has had a long and varied history with the Museum. He became interested in the institution when it was the "Museum of American Financial History," housed in the Standard Oil Building at 26 Broadway. After his first visit, he joined as a member and vividly recalls participating in a tour of the New York Mercantile Exchange for Museum members, during which the group had the opportunity to visit the palladium pits on the trading floor.

Andrew majored in math at Boston State College (subsequently incorporated into the University of Massachusetts at Boston) and obtained an MS in computer science from Marist College. Although his background is not in finance, he said he has been interested in the subject since his early teens, when he spent time on Wall Street while visiting his family in Queens.

Andrew's first job was as a YMCA youth director, after which he held positions in the computer departments of two companies prior to joining IBM in 1983. He worked at IBM for 31 years until his retirement on October 1, 2013, and he began volunteering at the Museum the following month. He holds the distinction of commuting the farthest of any volunteer — traveling over two hours from Poughkeepsie every Thursday to give tours to Museum visitors.

Andrew Schmidt (right) and Director of Education Chris Meyers on the NYSE floor.

At the Museum, Andrew particularly enjoys working with high school and college groups. "I really like giving them a sense of the importance of financial history, as well as Alexander Hamilton's place in society," he said.

In April, Andrew traveled much farther than his commute to New York City for the benefit of the Museum. He visited two North Carolina sites — the Reed Gold Mine in Carrabus County and the site of the original US Mint in Charlotte — to research an article for *Financial History* magazine. His article on the North Carolina Gold Rush is scheduled to run in the Summer 2016 edition of the magazine.

When he is not volunteering, Andrew enjoys traveling, especially to London, where one of his favorite sites is the Bank of England's money museum. He is also the treasurer of a walking club called the Volkssport Club at West Point and holds an Amateur Radio Extra Class license (call sign W2BOS). He is married, with two married daughters, an 18-month-old grandson and another grandchild on the way. $

SUMMER EVENTS

Jun 23 Ellen Feingold, curator of the Smithsonian's National Numismatic Collection on "The Value of Money." Talk followed by Q&A and book signing. 12:30 – 1:30 p.m. $5 includes Museum admission; members and students free.

Jul 12 Author Jeff Gramm on *Dear Chairman: Boardroom Battles and the Rise of Shareholder Activism*. Talk followed by Q&A and book signing. 12:30 – 1:30 p.m. $5 includes Museum admission; members and students free.

Jul 21 Damien Cregeau on "Mad Men in the Age of Downton Abbey: New York's Landmark Buildings in the Early 20th Century." Presentation followed by Q&A. 12:30 – 1:30 p.m. $5 includes Museum admission; members and students free.

Aug 17 Author and historian Edward Lengel on *First Entrepreneur: How George Washington Built His — and the Nation's — Prosperity*. Talk followed by Q&A and book signing. 12:30 – 1:30 p.m. $5 includes Museum admission; members and students free.

For more information or to register online, visit www.moaf.org/events.

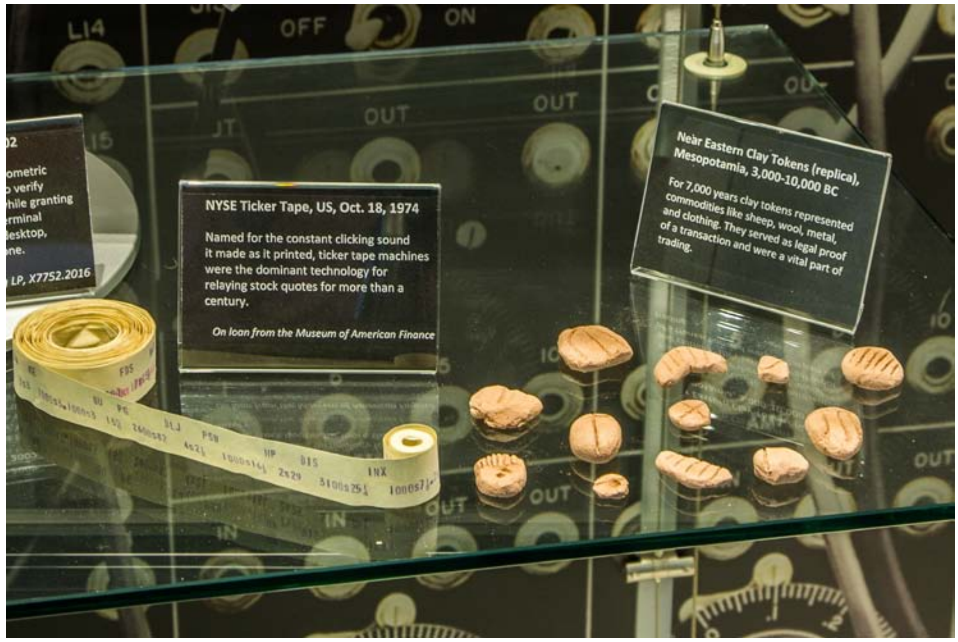
JUN 1 1999 Merrill Lynch announces that it is creating a fee-based financial planning business, in addition to its commission-based brokerage business, and that investors will also be allowed to trade stocks themselves through the company's website.

JUN 6 1934 The Securities Exchange Act is signed into law. It creates the US Securities & Exchange Commission (SEC) and requires companies to file registration documents with stock exchanges and to file quarterly financial statements with the SEC.

Securing Object Loans for Exhibitions

By Sarah Poole

In every issue of *Financial History*, we tell you the stories behind artifacts from the Museum's permanent collection. But what happens when the collection does not fulfill the needs of an upcoming exhibition? One option is to acquire new artifacts for the collection, but this is only viable if the items are readily available for donation or sale, are within the exhibition budget and fit the Museum's collecting mission. More frequently, the exhibition team relies on loans from other collections.



A handheld trading device and roll of ticker tape from the Museum's collection were featured in the Computer History Museum's *Tools of the Trade* exhibit.

Computer History Museum/Douglas Fairbairn Photography

We recently faced this challenge in developing the current temporary exhibition, *Worth Its Weight: Gold from the Ground Up*. This is the Museum's largest exhibition to date and features the highest number of objects on loan, with over 260 borrowed items on display. The 43 lenders that contributed to the exhibit consist of museums, private companies, universities and individual collectors.

The process for securing loans from other institutions can be lengthy. We began seeking out loans for *Worth Its Weight* more than a year prior to the exhibition opening. The first steps involve researching the collections of various institutions and identifying objects that fit the topics of the exhibition. As an Affiliate of the Smithsonian Institution, our exhibit team was able to visit the collections of various Smithsonian museums in Washington, DC, as well as to connect with other Affiliate museums across the country. The team was also referred to additional lenders through various professional networks, exhibit content advisors and exhibition sponsors.

Discovering interesting artifacts from potential lenders is one of the most exciting parts of creating an exhibit. Our research for the gold exhibit led us to gold dentures from the National Museum of Dentistry, a golden sword from the Arab American National Museum and even an example of the world's first gold coin from the private collection of Jonathan P. Rosen.

When requesting a loan from another museum, we typically must submit a formal letter or application, as well as a General Facility Report (GFR). The GFR is a standardized report developed by the American Alliance of Museums (AAM), a professional organization that sets best practices for museums in the United States. The report provides information about the physical specifications, environmental conditions and staff policies and procedures in place at a museum. This documentation clearly shows the level of care a museum will be able to provide for objects in its possession.

Once a loan is approved, the lenders and borrowers work together to ensure

JUN 9 1784 New York's first bank, The Bank of New York, opens for business at the Walton House in Lower Manhattan, only a few months after the British troops depart from American soil.

JUN 19 1969 The NYSE, so far behind on its antiquated paperwork that it has to close each Wednesday so clerks can process trades, appropriates the unprecedented sum of $7.5 million to upgrade its computer systems.

the safety of the loaned objects. Items will be hand delivered, if possible. Otherwise, they are professionally packaged for shipping. Condition Reports detailing any imperfections are performed by museum staff before and after shipping, and are repeated at the end of the exhibition. Lenders will also provide assistance in installing sensitive objects for exhibitions in order to ensure that the displays will not damage historic or delicate materials.

The benefits of object loans extends beyond single exhibitions. Lending programs often build reciprocal relationships between institutions, as well. For example, after securing the loan of three technological objects for the gold exhibit from the Computer History Museum, we sent two artifacts from our permanent collection to be displayed at their location in San Francisco. A handheld trading device and roll of ticker tape were featured in *Tools of the Trade* from October 2015 through January 2016. With this newly-forged relationship, we were able to spread our mission to museum-goers on the opposite coast.

The majority of objects in public and private collections around the world are not regularly displayed for the public. Largely due to constraints of time and space, many meaningful objects are preserved in collection storage. Through collaboration, museums can help bring these items to the forefront so that they can be exhibited and appreciated by our audiences. $

Sarah Poole is the Museum's Collections Manager. In addition to caring for the Museum's collection, she is also responsible for securing object loans for exhibitions.

Alan Barnett

The Museum's *Worth Its Weight* exhibit features more than 260 borrowed objects from 43 lenders.

JUN 27 1934 President Franklin D. Roosevelt enacts into law the National Housing Act and creates the Federal Housing Administration (FHA).

JUN 30 1934 President Roosevelt announces that he will name the notorious stock manipulator Joseph P. Kennedy the first chairman of the SEC.

Celebrating 20 Years

By Brian Grinder and Dan Cooper

We waited nervously in the library of the Museum of American Financial History — the former name of the Museum of American Finance — one brisk October afternoon in 1995. Several weeks earlier, we had received an email from New York University's Ed Altman. Dr. Altman had noticed an article we recently published in *Financial Practice and Education (FPE)* entitled "Applications of Financial History in the Teaching of Modern Finance." He wrote that he was on the board of a small financial history museum in New York City and that he had forwarded our article to the founder, John Herzog, who was interested in meeting us.

We didn't know who Mr. Herzog was, but as recently graduated Ph.D. students in finance from Washington State University, we were well aware of Dr. Altman's pioneering work on predicting bankruptcy. WSU, located in the hilly wheat fields of the Palouse in southeastern Washington, is a long way from New York, so we were honored when Dr. Altman noticed our work. Since we both planned to attend the Financial Management Association's annual meeting in New York City that October, we set up an appointment to visit the Museum while we were in town.

Our meeting with Mr. Herzog went well. He asked if the Museum's magazine, then called *Friends of Financial History*, could publish excerpts from our *FPE* article. Then he surprised us by asking if we would be interested in writing a regular feature for the magazine. We quickly agreed, and *Educators' Perspective* was born. We were excited but concerned about this new opportunity. Did we have enough material for four articles a year? We figured that we were good for about two years. After that, who knew?

The *Educators' Perspective* column first appeared in the Spring 1996 edition of this magazine, then called *Friends of Financial History.*

After our meeting, we viewed the Museum's exhibits, which at the time were located in a stairwell in the Standard Oil Building at 26 Broadway. Dr. Altman wasn't kidding when he described the Museum as small! One exhibit in particular caught our eye; it featured Hetty Green, known as "The Witch of Wall Street." Neither of us had ever heard of Hetty Green. Her story fascinated us, and it gave us our first topic for the new *Educators' Perspective* column. Our article, "Hetty Green: Legendary Wall Street Investor," was published 20 years ago in the Spring 1996 edition. It not only inaugurated the new feature in the magazine, but it also gave us material to use in our classrooms that enabled us to broach the topic of the role of women in business and finance. This

led to some very interesting classroom discussions over the years.

Two years passed quickly and, to our relief, we realized we hadn't come close to running out of material for our column. These articles have been a joy to write, and they have been extremely useful within the classroom. For instance, "Depreciation Goes to War" (Fall 1996) is a great way to introduce the concept of depreciation in an introductory finance course. Likewise, "The Playboy and the Radium Girls — Part 1" (Spring 2008) is an effective, if somewhat morbid, example of diversifiable risk. At least two articles provide excellent examples of the pitfalls and practices of capital budgeting: "The XIT Ranch of Texas: A Capitol Capital Budgeting Project" (Winter 2010) and "Turning a Yankee Liability into an Asset: Selling New England Ice in India, 1833-1880" (Fall 2012).

In the area of personal finance, the articles "Financing the American Dream: A History of the Fully-Amortized 30-Year Mortgage" (Spring 2015) and "Overcoming Resistance to Life Insurance in the 19th Century" (Fall 2004) offer students unique perspectives on these topics that can't be found in the typical personal finance textbook.

Beyond the classroom, we hope the readers of *Financial History* have found our *Educators' Perspective* columns to be entertaining and informative. As academics, we are painfully aware of the tendency for financial economists to ignore history in their writing and emphasize tedious mathematical equations or arcane statistical methods that leave most readers gasping for air. Our aim with every *Educators' Perspective* article is to provide readers with a deeper appreciation for the perspective history provides to anyone wishing to understand financial markets.

The topics we have covered over the span of the last two decades have been wide-ranging and sometimes unexpected. *Educators' Perspective* has addressed everything from chickens to Theodore Roosevelt. Scott Joplin's *Wall Street Rag*, the American West, gambling, the Dust Bowl, Billy Wilder movies, the Biltmore Estate, Charles Dickens, short squeezes, changes in

20 Lessons From 20 Years of *Educators' Perspective*

1. Financial history matters.
2. The Empire State Building was a construction marvel but a financial disaster. (Issue 65, 1999 I)
3. We can thank gamblers for the development of statistics. (Issue 93, Winter 2009)
4. Alexander Hamilton's nemesis, Aaron Burr, founded the Bank of the Manhattan Company. JPMorgan Chase & Co. traces its beginnings to Burr's fledgling institution. (Issue 89, Fall 2007)
5. Director Billy Wilder understood risk better than most finance professors do. (Issue 98, Fall 2010)
6. Music, with its ability to express emotion, has an extraordinary ability to capture the moods, cadences and rhythms of financial panic. (Issue 59, Summer 1997)
7. The word "mortgage" comes from an Old French word meaning "dead" and an Old Germanic word meaning "pledge." Thus, a mortgage is a "dead pledge!" (Issue 113, Spring 2015)
8. It's possible to ship ice from New England to India in a wind-powered sailing vessel without refrigeration. (Issue 104, Fall 2012)
9. Texas got a great deal when it traded land in the Texas Panhandle for a new capitol building. (Issue 96, Winter 2010)
10. Charles Dickens hated compound interest. (Issue 110, Spring 2014)
11. There once was a speculative chicken bubble. (Issue 114, Summer 2015)
12. Never take investment advice from an academic. (Issue 92, Fall 2008)
13. The flow of information has always been important to financial markets. (Issue 60, Fall 1997)
14. Financial acumen is not hereditary; Hetty Green's children squandered her fortune. (Issue 55, Spring 1996)
15. Depreciation played an important role in preparing the United States for entry into World War II. (Issue 57, Fall 1996)
16. Wall Street got a small taste of the Dust Bowl in May of 1934 when a dust storm darkened the skies for about five hours and dumped an estimated 40 tons of dust per cubic mile on the city. (Issue 95, Fall 2009)
17. Huguette Clark, the daughter of the "Copper King" William Andrews Clark (1839–1925) died in 2011 in New York City at the age of 104. (Issue 106, Spring 2013)
18. John D. Rockefeller, Sr. was no fan of competition. (Issue 111, Fall 2014)
19. A lot of financial history happened in Montana! (Issue 64, 1998 IV; Issue 84, Fall 2005; Issue 97, Spring 2010; Issue 105, Winter 2013; Issue 106, Spring 2013; Issue 107, Summer 2013)
20. The Spanish Conquistadors were not professional soldiers. Their ventures into the New World were more entrepreneurial than military in nature. (Issue 116, Winter 2016; and forthcoming)

technology, Eddie Cantor's *Caught Short!: A Saga of Wailing Wall Street* and modern day bucket shops have all appeared in our column. We hope such a diversity of topics has been relevant and enjoyable.

One of the unexpected benefits of our association with the Museum has been the opportunity to work with some of Wall Street's finest. We have both served on *Financial History's* Editorial Advisory Board, and Dan was a member of the Museum's Board of Trustees for several years. In that capacity, we have met and worked with fellow academics, Wall Street practitioners and financial media specialists. As finance professors at small regional institutions, we have been so very thankful for this rare opportunity.

Our respect and admiration for Mr. Herzog and the institution he founded has only increased with each passing year. We are also grateful to the Museum's staff for its continued support, with special thanks to *Financial History* editor Kristin Aguilera, who has put up with our late submissions and discovered wonderful illustrations for our articles.

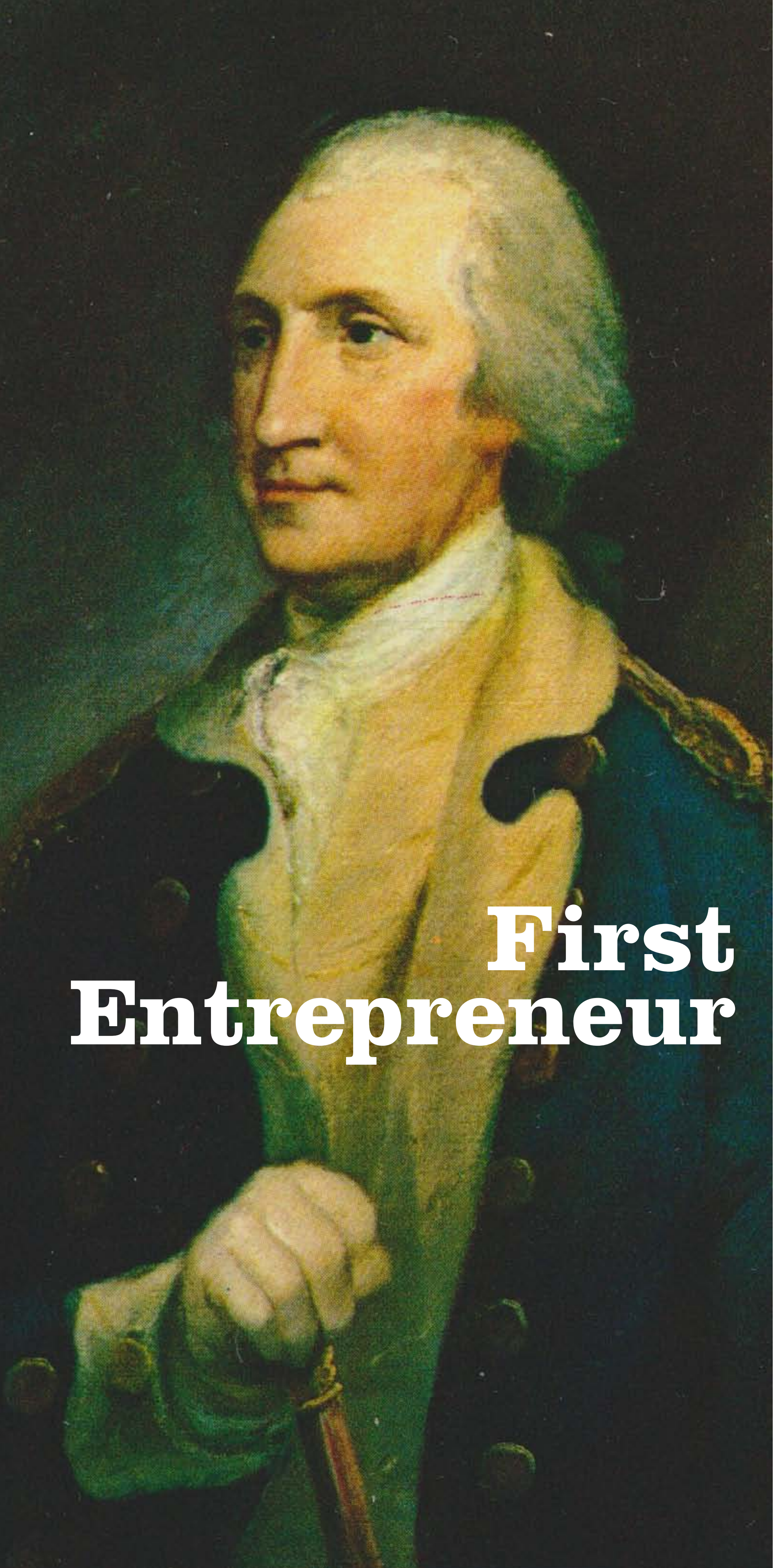
Over the years, the name of the Museum has changed, as has the name of the magazine, and the Museum has moved and expanded several times since we first visited the exhibits at 26 Broadway. What has not changed is the Museum's dedication "to preserving, exhibiting and teaching about American finance and financial history." We hope our column has contributed in some small way to that mission. $

Brian Grinder is a professor at Eastern Washington University and a member of Financial History*'s editorial board. Dr. Dan Cooper is the president of Active Learning Technologies.*

Source

Grinder, Brian, and Dan W. Cooper. "Applications of Financial History in the Teaching of Modern Finance." *Financial Practice and Education* 5, 96–106. 1995.

First Entrepreneur



By Edward G. Lengel

George Washington probably wrote thousands of safe-passage passes, as was only natural for a man who held so much authority. Most of them were routine: allowing civilians to cross military checkpoints, messengers to enter secured areas, and the like. There were exceptions — like passes for spies. None, though, was more unusual than the one he penned at his presidential desk in Philadelphia on the morning of January 9, 1793. It read:

> The bearer hereof, Mr. Blanchard a citizen of France, proposing to ascend in a balloon from the city of Philadelphia, at 10 o'clock, A.M. this day, to pass in such direction and to descend in such place as circumstances may render most convenient — These are therefore to recommend to all citizens of the United States, and others, that in his passage, descent, return or journeying elsewhere, they oppose no hindrance or molestation to the said Mr. Blanchard; And, that on the contrary, they receive and aid him with that humanity and good will, which may render honor to their country, and justice to an individual so distinguished by his efforts to establish and advance an art, in order to make it useful to mankind in general.

Washington would deliver this pass personally. Cannon fire awoke Philadelphians at dawn that day. The guns — unloaded, thankfully — boomed at regular intervals thereafter, and a growing hubbub embroiled the streets. Curious crowds gravitated toward the prison yard, where people jabbered excitedly about a big event due to begin at nine o'clock. Many probably thought they were about to witness a hanging until they caught glimpses of an immense heap of yellow varnished silk laced with netting lying in the yard's center. A Frenchman gaily dressed in a

General George Washington, later the nation's first president, was also an early entrepreneur who believed the world needed visionaries.

blue suit and cocked hat bedecked with white feathers strutted around the heap, looking important. Incredibly, the heap began to expand slowly as an orchestra played a slow, solemn accompaniment. Soon an "immense concourse of spectators" had assembled to view the "majestic sight," which they found "truly awful and interesting." Discovering that the heap of cloth was in fact a balloon, and that they were about to witness it in flight, the crowd broke into frenzied applause. Some noticed men hawking tickets — five dollars to enter the prison yard and witness the spectacle up close. This crowd, though, possessed a sort of collective intelligence. Reasoning that once the balloon ascended it would be just as visible from outside the yard as it was inside, spectators spurned the ticket-sellers and scrambled onto window ledges, shimmied up posts and stampeded into nearby vacant lots.

At 10 o'clock another finely dressed and solemn figure entered the yard — the President of the United States. Washington handed his pass to "the bold Aeronaut" and spoke a few words into his ear. After a simple bow, the Frenchman vaulted with amazing agility into his "blue and spangled" boat under the now fully-inflated balloon. While the President watched, he dumped some ballast and the craft slowly began to rise. Blanchard furiously waved flags of the United States and France, and then waved his hat to "the thousands of [mostly freeloading] citizens from every part of the country who stood gratified and astonished at his intrepidity." The wind swept up within a few minutes, propelling the balloon off to the southeast. Some local gentlemen whipped their steeds after it but fell quickly behind as it disappeared over the treetops.

Blanchard's intended destination is uncertain, but his balloon landed in a field east of Woodbury, New Jersey. From there he hitched a ride on a passing carriage, arriving back in Philadelphia later that evening. As soon as he entered the city, the Frenchman hurried "to pay his respects to the President of the United States." He told Washington — always a lover of details — that he had spent 46 minutes aloft and covered 15 miles. The President congratulated him and turned back to the business of running the country while Blanchard left to square his accounts. What he discovered astonished him. After all the money that he had invested in preparing the balloon and staging a grand spectacle — those artillerymen and musicians all had to be paid — Blanchard's ticket receipts had been miserable. In a single blow he had lost several hundred dollars. He would have to beg for donations just to get back to France.

This amusing but rather sorry event was not Washington's first exposure to lighter-than-air flight. Back in 1784 he had read accounts of balloon flights in Paris, prompting him to joke to the Marquis de Lafayette that he might eventually fly across the Atlantic to "make you a visit in an air Balloon in France." Learning that French adventurers proposed to conduct similar flights in the United States, Washington was curious — but determined that nothing on earth would ever get him up in a balloon. "It may do for young men of science & spirit to explore the upper regions: the observations there made may serve to ascertain the utility of the first discovery, & how far it may be applied to valuable purposes," he wrote on November 25, 1785, to his Irish friend Edward Newenham.

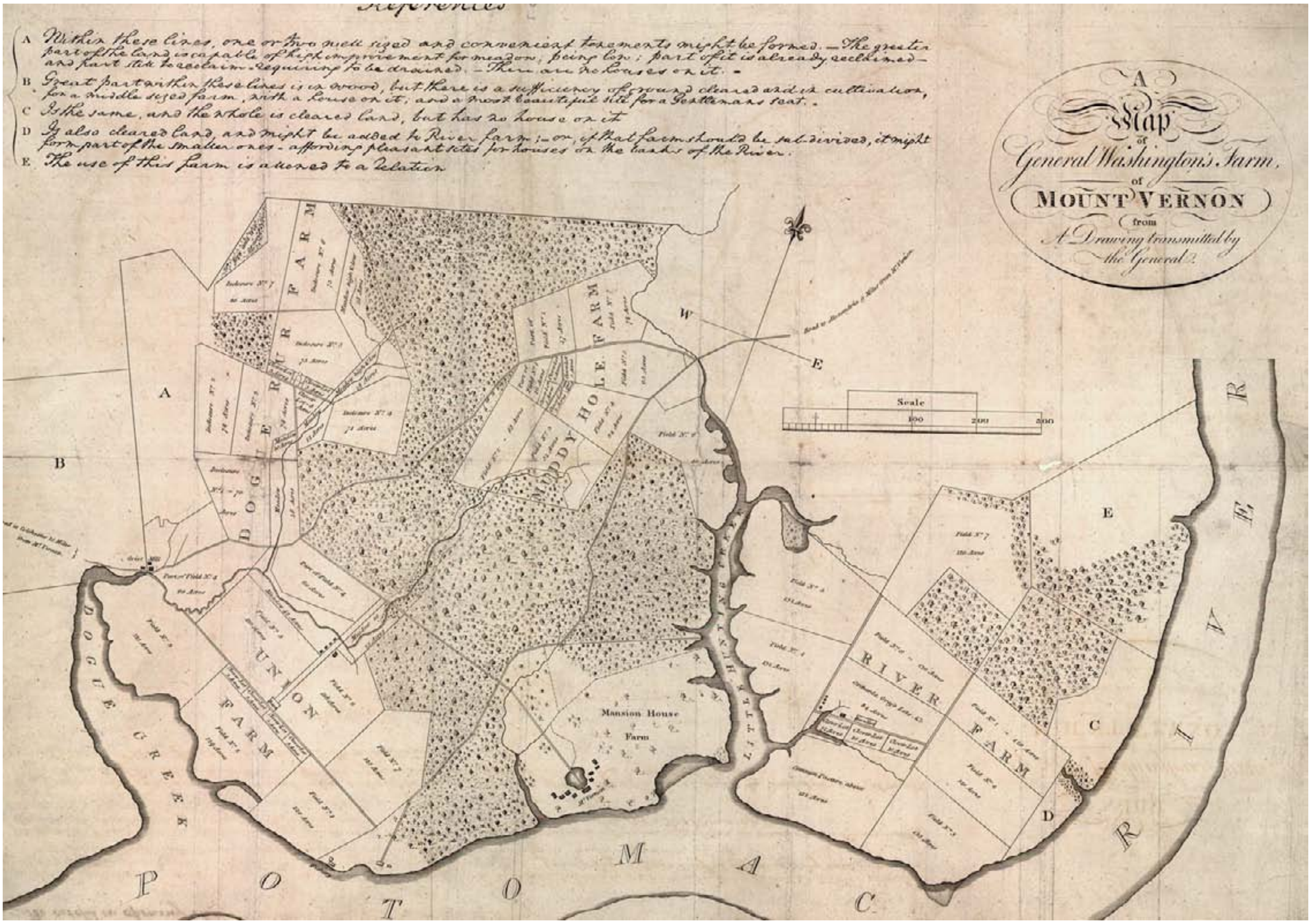
Bettmann / Contributor

Illustration of George Washington surveying land. His first income came from the salary he earned as a surveyor.

"To such alone I think these voyages ought at present to be consigned — & to them handsome public encouragements should be offer'd for the risk they run in ascertaining its usefulness, or the inutility of the pursuit." The world needed visionaries — but always with an ample helping of prudence. He might have said the same about the management of his own wealth, and the economy of the United States.

Washington was a crafty and diligent entrepreneur. He began early, employing principles imbibed from his parents, family, and friends to build his fortune. His first income came from the salary he earned as a surveyor. Saving and investing, he used this to purchase land and grow tobacco. A modest inheritance helped to establish him as a substantial landowner and gifted him with an estate — Mount Vernon — that became his country seat. Marrying Martha Dandridge Custis, a wealthy widow who would become his devoted partner, George acquired the wherewithal to begin operations on an exalted scale.

Today, the word "farmer" has humble connotations. Washington was anything but. Driven by a powerful (but not ruthless or obsessive) ambition, he transformed his estate from a tobacco plantation mired within an oppressive colonial system into a profitable enterprise producing



Library of Congress

Map of George Washington's farm at Mount Vernon, based on his own drawings.

commodities for trade throughout America, the West Indies, and Europe. Hard work—for he viewed industry as both a natural and a moral quality—built his fortune. But so did practices he learned through instruction and experience: prudence, attention to detail, transparency, clear and active communication, honesty, experimentation and boldness tempered by thrift. Washington's progress toward personal wealth — he left behind a sprawling estate of over 50,000 acres and almost achieved millionaire status at a time when the distinction was rare indeed — makes up part of his story.

Even as he grew personally wealthy, Washington set the course for national prosperity. His personal experiences and abilities as an entrepreneur inspired his policies both as general and as President. Such was the case with his dread of debt. Unfortunately for posterity, Washington never kept a dream journal. In his nightmares, he was probably pursued by hordes of bayonet-wielding redcoats or hounded by Thomas Jefferson and his baying minions of the press. More frequently, Washington must have woken up drenched in sweat after dreaming that he had opened up his account books to discover his estate swamped by unsustainable debt. He spent the balance of his life straining to keep this dreadful experience from becoming reality for either himself or his country. Other principles guiding his economic policies included fiscal stability, national unity and peace. Never, though, did he aspire to command prosperity. He thought of the economy as a kind of self-sustaining machine.

Government's job was to keep it clean, well-oiled and secure. The people fueled it, set it in motion and — after a tithe to the government to fund its expenses — reaped the benefits. The operation was both natural and simple. Always, though, he exhorted the people to keep one principle in mind: work together, or perish separately. Washington was the unifier to guide them. $

Edward G. Lengel is an American military historian and professor at the University of Virginia. He is the director of the Washington Papers documentary editing project in Charlottesville, VA. Adapted excerpt from First Entrepreneur: How George Washington Built His — and the Nation's — Prosperity *by Edward G. Lengel. Copyright © 2016. Available from Da Capo Press, an imprint of Perseus Books, a division of PBG Publishing, LLC, a subsidiary of Hachette Book Group, Inc.*

DOING WELL BY DOING GOOD

By Gregory DL Morris

During the recession of 2009–10, the term "financial engineering" got a very bad reputation. It became synonymous with deliberately opaque and convoluted instruments designed to fool investors and regulators. But not all financial engineering is deceptive and daedal. Every element of finance, from fiat money to common stocks, had to be invented.

That invention continues. One of the more recent innovations was designed to reduce risk, rather than increase it, and has been by all accounts very successful. Catastrophe bonds, or cat bonds, were developed in the 1990s to address several important needs in the risk-transfer sector.

A series of monster events severely stressed the capacity of even the largest underwriters and the reinsurance companies that backed them. They sought not just ways to increase their capacity, but also ways to apportion risk beyond traditional markets. At the same time, smaller firms were interested in participating in larger markets and risks, but in limited ways. Further, capital markets were eager for non-correlated, alternative investments.

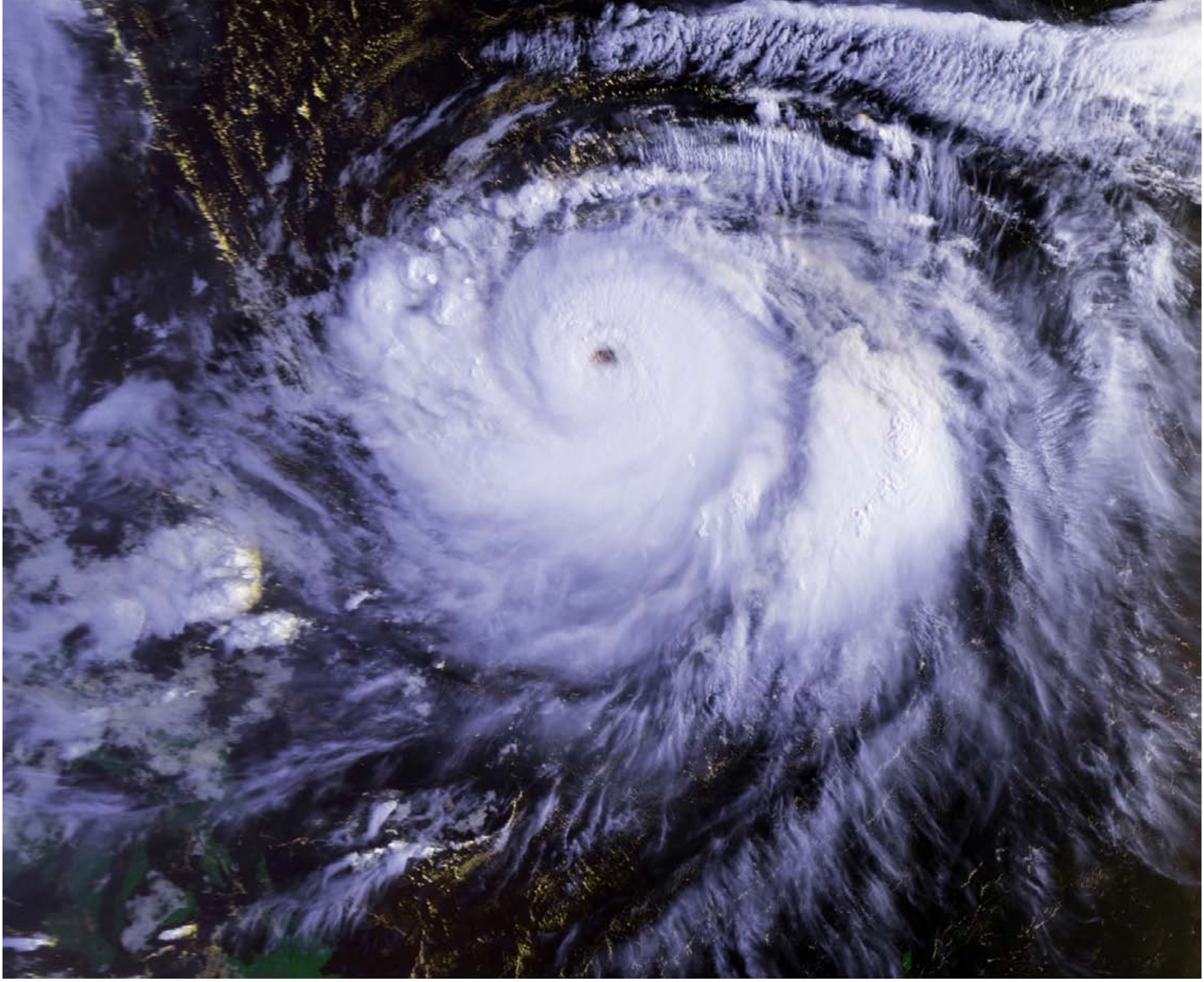
"There had been attempts to create a market in exchange-traded index instruments on the Chicago Board of Trade in the early 1990s," said Dirk Lohmann, CEO and managing partner of Secquaero Advisors, based in Zurich.

The galvanizing event for what became cat bonds was Hurricane Andrew in 1992. "That was a market-changing event," Lohmann said. "A lot of insurers and reinsurers did not use probabilistic models in those days, although they did exist and were available for commercial license."

Hannover Re was an early adopter of such models under Lohmann's guidance.

Today the global market for cat bonds is about $25 billion. There is an even larger market, about $70 billion in broader alternative capital for risk transfer. That

Aftermath of Hurricane Andrew, which hit Florida in 1992 and sparked the idea for catastrophe bonds.



National Oceanic and Atmospheric Administration

Typhoon Mireille — shown here at peak intensity on September 22, 1991 — caused $10 billion in damage in Japan and Korea.

comprises private transactions, swaps and collateralized structures, as well as peer-to-peer arrangements. Lohmann's firm, Secquaero, handles about $2 billion a year in insurance-linked securities.

Lohmann began his career with Hannover Re in 1980. He spent a total of 17 years in various capacities up through member of the executive board. During his time with Hannover, Lohmann played a large role in the company's growth from that of a following reinsurer — one that does not quote the original business but takes a minority position in club deals and syndications — into the world's fifth largest reinsurer. He then held leadership positions at various firms in the industry until forming Secquaero Advisors in 2007.

Lohmann was an early pioneer in the field of insurance securitization, having personally negotiated and placed the world's first non-life insurance securitizations, called Kover, in 1993–94. Each of the transactions he was involved in included several firsts in that emerging field. In 1996, the K2 Portfolio Swap saw the first use of a standard master swap agreement certified by the International Swaps and Derivatives Association to transfer the risk and performance of an underlying defined portfolio to investors rather than relying upon a special-purpose vehicle structure.

On its own, Hurricane Andrew was the largest single insured loss in history to that time, with totals estimated between $18 and $25 billion. But Lohmann said that Andrew came after several other global-scale losses: severe winter storms across Europe in 1990 and Typhoon Mireille, which hit Japan and South Korea in September 1991, causing $10 billion in damage. It remains one of the worst non-Atlantic storms in terms of damage. For reference, Hurricane Katrina caused an estimated $45 billion in insured losses in 2005.

So many massive losses overwhelmed the insurance and reinsurance business, and some underwriters were left insolvent. For the survivors, capital was scarce. Premiums and fees shot up, while capacity to underwrite further risks tumbled. But nature abhors a vacuum, and that led to new insurance markets being developed, such as the one that thrives today in Bermuda.

"At that time we were already in the top six or seven reinsurance firms in the world," Lohmann said, "and even we were capital constrained. We were 100% owned at the time by a German mutual, and we were actually larger than our parent. So we started exploring alternative sources of capital. We started discussions with banks and developed an insurance-linked note

in which performance was determined by a designated portfolio of risks; risks that were modeled. It was not a single-event instrument, but a portfolio."

Hannover worked with the exotic derivatives group at Citibank and created a reinsurance agreement with a Cayman-domiciled special purpose reinsurer that issued $100 million in principal-at-risk notes to investors. The whole process was long and complex, taking from July 1993 to January 1994.

"Reinsurance is known to be driven by custom and practice," Lohmann said. "There is a standard reinsurance agreement that runs 12 pages. By the time we were done, the new reinsurance agreement itself ran to 72 pages. All of the supporting agreements — payment agent, escrow agreement, calculation agent and so forth — filled two binders. Everything had to be defined."

It was also very expensive. "I think we ran up 500,000 pounds sterling in legal fees," Lohmann said. "But we knew we were breaking new ground. We knew we were setting a new standard."

It took a couple of years for the performance of that first structure to be seen in action, and also for others to review the terms and conditions. Lohmann noted that the next structure, George Town Re created at the end of 1997, "mirrored our arrangement," and was tradable under securities Rule 144A. According to industry resource Artemis, George Town was done by St. Paul Re as cedent/sponsor and Goldman Sachs as placement/structuring agent.

"Cat bonds are a very precise sub-form of alternative financing in the reinsurance market through risk transfer," said Axel Wichmann, senior underwriter with Hanover Re.

Wichmann said there are broadly two structures in the reinsurance market, proportional and non-proportional. Proportional is where an underwriter takes on business, and then farms out some of that on a 1:1 basis. The other firm might get 20% of the revenue and be on the hook for 20% of any claims. This structure, sometimes known as a sidecar, is used to expand capacity.

A non-proportional structure is protection for both insureds and underwriters against large losses. It covers losses above the limits of what an insurer can normally accommodate. These options include cat bonds.

Axel Wichmann, senior underwriter with Hanover Re.

"The first form of transferring risks on a proportional basis was developed in the mid-1980s," Wichmann said. Hanover Re was a pace setter among reinsurance firms that had been ambitious in developing new business. "The reinsurance companies had access to business that smaller companies did not, and they wanted to. Eberhard Mueller [who was head of the mathematics and statistics department] said we could just write more business and send out some at the back end. The partners would come on proportionately and pay just a bit for the work we do to originate business."

Hannover was "assessing many types of risk at the time," Wichmann said. "There was great innovation and evolution. We were diversifying and adding capacity. There was an evolution of the big players."

"Proportional systems allow companies to accept business that they would not be able to accept otherwise for capacity constraints or other restrictions," Wichmann said. "It is more a capacity tool than a protection. It also helps diversify risk and helps other players get access to business that they could not get otherwise."

Cat bonds and other forms of alternative financing/risk transfer are the equivalent of non-proportional coverage arising in capital markets, not the insurance market. As is often the case, it took a couple of big losses for the insurance community to realize that new approaches were necessary for massive claims.

"If every loss were just as expected, we might not need cat bonds and alternative capital," Wichmann said. "Then there was Hurricane Andrew in 1992 and Katrina in 2005. Those were different than the models told us. We learned the possibility that losses could be much bigger than we had thought. In insurance, the next event sometimes shows you what you didn't think of."

According to Wichmann, those low-occurrence, high-risk exposure events don't fit well into the traditional reinsurance model where insured values accumulate to undesired levels, but are ideal for capital markets and institutional investors. The losses are big, but infrequent. And, importantly, they are triggered and paid relatively quickly — within two or three years.

"Those are just the opposite of many traditional risks in the reinsurance market, like liability risks for example," he said. "Reinsurers don't mind if the claim is open for 30 years."

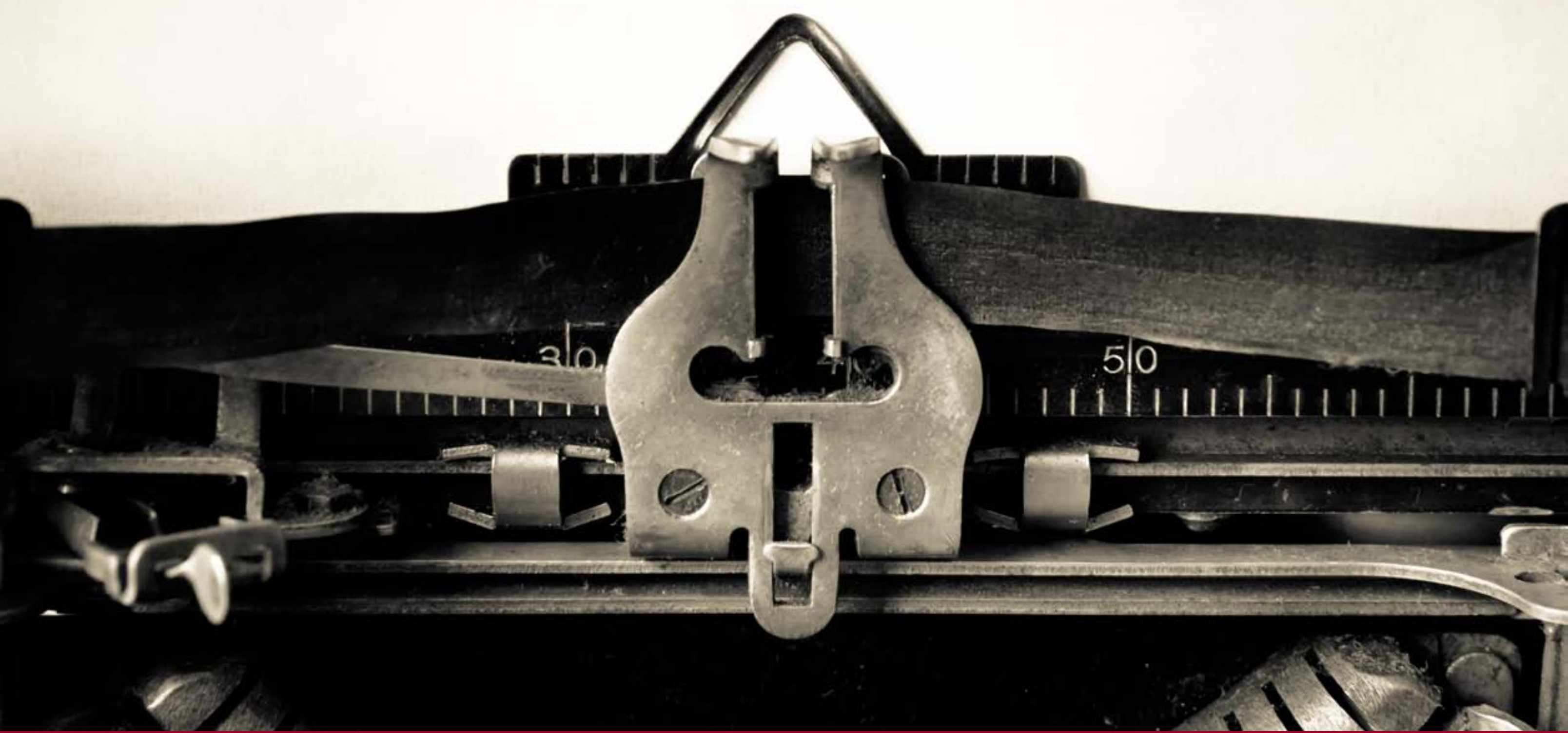
With cat bonds and alternative capital, investors set quick and simple rules, usually with a parametric trigger and fixed or graduated payments. That means actual losses do not have to be proven in many cases. Rather, the payment is triggered by external conditions, such as amount of rain, barometric pressure or storm surge as measured over a given time at specific places.

One recent example is Hurricane Hugo that hit Mexico. The parametric triggers indicated a 50% payout for that storm, even though actual property damage was minimal.

"The key year in development of alternative capital was 1994," Wichmann said. "We took part in the first securitization that took excess coverage out to the capital markets. Our structure at the time was called Kover, so the securitization was K-1. We have since gone up through K-6 and now just K." $

Gregory DL Morris is an independent business journalist, principal of Enterprise & Industry Historic Research (www.enterpriseandindustry.com) and an active member of the Museum's editorial board.

Dear Chairman



Boardroom Battles and the Rise of Shareholder Activism

By Jeff Gramm

Public companies are filled with contradiction and conflict of interest. The best place to study these peculiar institutions is at the fault line where shareholders and corporate managers and directors meet. I've always kept a collection of "Dear Chairman" letters on my desk. To me, each one is a fascinating example of capitalism at work; the critical point at which a shareholder decides to engage management, distilled into a letter. The business world can be a messy place, and there is perhaps no better way to understand it than to study its many conflicts. These letters teach us how American business really works, through the voices of its most interesting participants.

Robert R. Young and the Proxyteers

The proxy fight for the C&O Railway sent a warning shot through public company boardrooms across the country. Robert R. Young, whom the *Saturday Evening Post* would later call "The Daring Young Man of Wall Street," bested Guaranty Trust and, allegedly, J.P. Morgan, not with ample supplies of capital, but merely by lobbying public shareholders.

He also caught the attention of a handful of aggressive young men who were beginning to build their own business empires during the Great Depression. Young's campaign for the C&O Railway taught them a winning strategy for seeking control of public companies by proxy vote. When the US economy began to expand after the end of World War II, they worked from Young's playbook to target underperforming public companies, including major railroads and other household names such as Montgomery Ward, Decca Records, 20th Century–Fox and MGM-Loews. This group of feared raiders picked up a name in 1951, when the management of United Cigar–Whelan Stores Corporation labeled Charles Green a "Proxyteer."

The 1950s were bountiful for investors. The decade remains one of the Dow Jones Industrial Average's best ever, with a 240% gain. The '50s also saw significant changes in the ownership structures of public companies. Wall Street vigorously promoted broad share ownership with efforts such as the New York Stock Exchange's

"Own Your Share of American Business" campaign. The Proxyteers put this propaganda to the test. They bought large interests in public companies, often from vestigial holders liquidating their stakes, and they attacked management teams in the name of shareholders' rights. Managers were incredulous. Often the CEO's first response was simply a befuddled, "Who? I have never heard of this guy." But the Proxyteers were not easily dismissed. As Charlie Green said, "If owning stock doesn't make me a partner, then all that stuff they hand out about how if you own shares you're a partner in American business is a lot of baloney."

The New York Central Proxy Fight

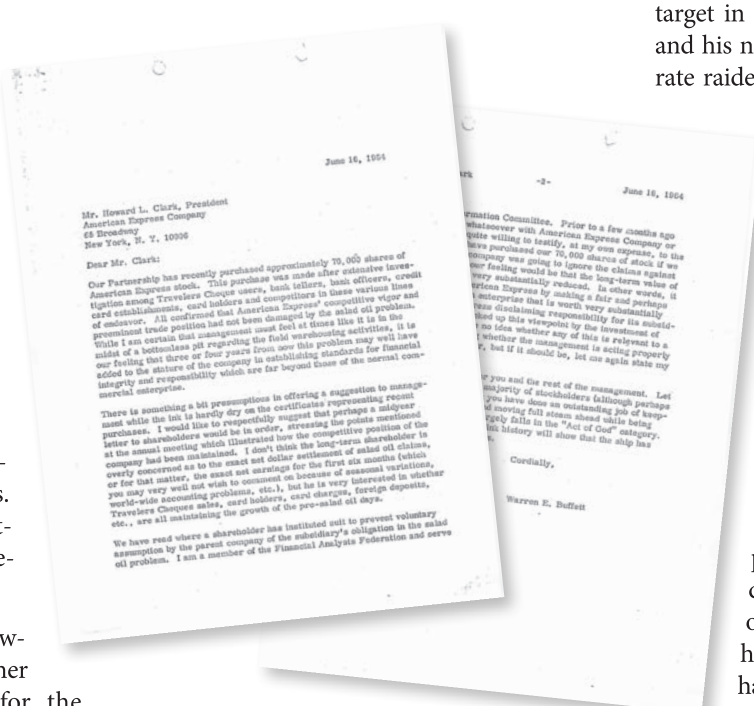
When "Commodore" Cornelius Vanderbilt won control of the New York Central in 1867, he did it via cutthroat competition and behind-the-scenes share purchases. Almost 90 years later, when Young began his own assault, he courted the common shareholder. He did so with a flair for the dramatic, turning shareholder communiqués from formal legal documents into entertaining and irreverent missives. One of his most provocative letters to New York Central shareholders read:

> WARNING: If any banker, lawyer, shipper, supplier or other person solicits your proxy for the present Board, ask him what his special interests are, or what your Company is paying for his services. Like the bankers now on your Board, he, too, may be hoping to receive special favors from your railroad or from the bankers.

Young was the elder statesman of the Proxyteers, and the New York Central fight was the culmination of his decades-long battle against the Wall Street establishment. He had already made his fortune and built his mansions in Palm Beach, Florida and Newport, Rhode Island. But the New York Central was the ultimate trophy—his chance to win the Vanderbilts' railroad at the expense of the Morgans and their ilk.

Warren Buffett and the Great Salad Oil Swindle

The Great Salad Oil Swindle was an audacious fraud that nearly toppled American Express in the 1960s. It is a complicated story filled with valuable lessons about the fallibility of businessmen and their capacity to ignore reality at critical junctures. While the saga exposes terrible behavior and a true villain, it features many more honest and capable people who unwittingly developed deadly blind spots. The fallout from the fraud also pitted Warren Buffett against a handful of shareholders who wanted American Express to maximize its short-term profits by ignoring salad oil claimants.



June 16, 1964

Mr. Howard L. Clark, President
American Express Company
65 Broadway
New York, N. Y. 10006

Dear Mr. Clark:

Our Partnership has recently purchased approximately 70,000 shares of American Express stock. This purchase was made after extensive investigation among Travelers Cheque users, bank tellers, bank officers, credit card establishments, card holders and competitors in these various lines of endeavor. All confirmed that American Express' competitive vigor and preeminent trade position had not been damaged by the salad oil problem. While I am certain that management must feel at times like it is in the midst of a bottomless pit regarding the field warehousing activities, it is our feeling that three or four years from now this problem may well have added to the stature of the company in establishing standards for financial integrity and responsibility which are far beyond those of the normal commercial enterprise.

There is something a bit presumptious in offering a suggestion to management while the ink is hardly dry on the certificates representing recent purchases. I would like to respectfully suggest that perhaps a midyear letter to shareholders would be in order, stressing the points mentioned at the annual meeting which illustrated how the competitive position of the company had been maintained. I don't think the long-term shareholder is overly concerned as to the exact net dollar settlement of salad oil claims, or for that matter, the exact net earnings for the first six months (which you may very well not wish to comment on because of seasonal variations, world-wide accounting problems, etc.), but he is very interested in whether Travelers Cheques sales, card holders, card charges, foreign deposits, etc., are all maintaining the growth of the pre-salad oil days.

We have read where a shareholder has instituted suit to prevent voluntary assumption by the parent company of the subsidiary's obligation in the salad oil problem. I am a member of the Financial Analysts Federation and serve

-2-

June 16, 1964

...rmation Committee. Prior to a few months ago ... whatsoever with American Express Company or ... quite willing to testify, at my own expense, to the ... have purchased our 70,000 shares of stock if we ... company was going to ignore the claims against ... our feeling would be that the long-term value of ... very substantially reduced. In other words, it ... erican Express by making a fair and perhaps ... enterprise that is worth very substantially ... ress disclaiming responsibility for its subsid... ked up this viewpoint by the investment of ... no idea whether any of this is relevant to a ... whether the management is acting properly ... r, but if it should be, let me again state my

... r you and the rest of the management. Let ... majority of stockholders (although perhaps ... you have done an outstanding job of keep... d moving full steam ahead while being ... rgely falls in the "Act of God" category. ... ink history will show that the ship has ...

Cordially,

Warren E. Buffett

Letter from Warren Buffett to American Express President Howard Clark regarding the company's involvement in the 1960s Salad Oil Swindle.

When Buffett intervened at American Express as a large shareholder, he didn't demand board representation or ask probing questions about the company's operating performance. He didn't call for a higher dividend or question the company's capital spending. Instead, he wanted American Express to use its capital liberally to recompense parties who were defrauded in the swindle. Buffett had done enough research on American Express to understand that it was a phenomenal business. He would later refer to companies like this as "compounding machines," because they generate huge returns on capital that can be reinvested at the same rate of return. Buffett knew that walking away from the salad oil claims would damage American Express's reputation and its substantial long-term value. He wanted to prevent short-term-oriented shareholders from jamming the compounding machine's gears just to save a few dollars.

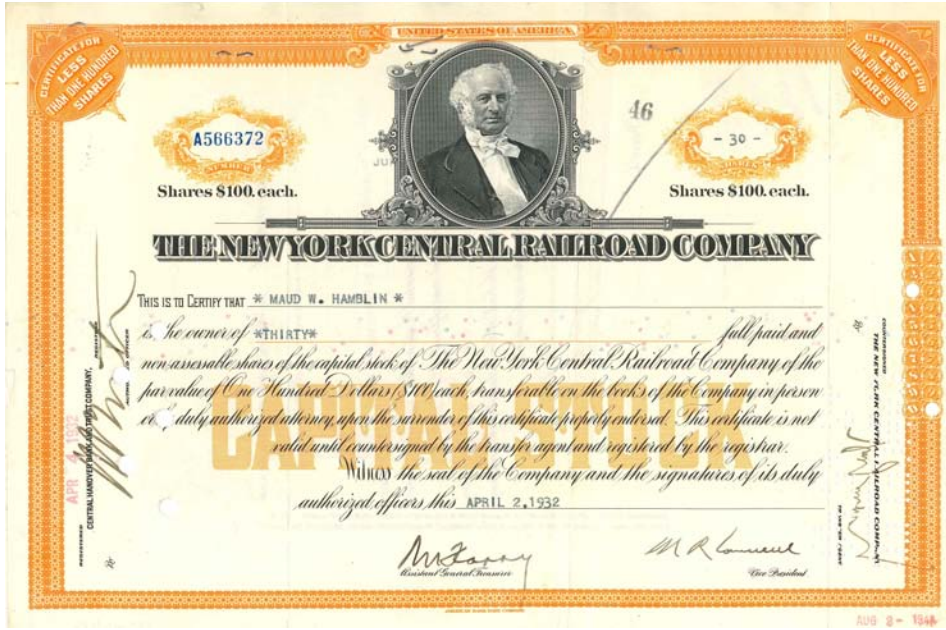
Carl Icahn's Bear Hug of Phillips

On February 4, 1985, Carl Icahn sent a letter to William Douce, chairman and CEO of Phillips Petroleum, offering to buy the company. He wrote that if Phillips did not accept his bid, he would launch a hostile tender offer for control. Phillips was Icahn's 15th target in his seven-year career as a raider, and his note to Douce was a classic corporate raider's "bear hug letter"—an offer to purchase the company, followed by threats should he be ignored. While Icahn had used the same playbook for his earlier battles, this showdown was markedly different: Phillips was one of the largest corporations in the world, many times bigger than any company he had ever pursued.

Icahn once said of his early corporate raids that he was merely "playing poker." He borrowed heavily to fund his stock purchases, and his threats to tender for controlling stakes were often bluffs. He explained, "I didn't have the money to fight for the long haul—to pay the interest on the shares I held." When Icahn threatened an $8.1 billion tender offer to take control of Phillips, few people took him seriously. Phillips's investment banker, Joe Fogg, told him, "That's preposterous. What the hell do you know about the oil business?" Phillips, which had just endured an intense fight with raider T. Boone Pickens, ran full-page newspaper ads asking, "Is Icahn for Real?" This time, he was. "Cash! We have cash," he responded to Fogg. "We'll hire people who know about the oil business."

The 1980s Deal Decade

America's fourth great merger wave proved to be much more substantial than its conglomerator-driven predecessor. The 22,000 mergers and acquisitions of the



New York Central Railroad stock certificate, dated April 2, 1932. The certificate bears the image of "Commodore" Cornelius Vanderbilt, who won control of the railroad in 1867 via cutthroat competition and behind-the-scenes share purchases.

Collection of the Museum of American Finance

1980s "deal decade" included leveraged buyouts by private equity firms, strategic acquisitions by corporations taking advantage of lax antitrust enforcement and expansion into the US market by international companies. But it was the hostile takeovers — though they made up only a small percentage of the decade's deals — that defined Wall Street in the '80s.

That the public was so taken by battles between such unsympathetic figures says something about the high stakes and drama of hostile takeovers of that decade. A few people may have looked on with disgust as vulture raiders pecked at fat cat CEOs, but for everyone else, these clashes at the top of our largest companies were Hollywood material.

Thirty years earlier, nobody really knew what to make of fledgling corporate raiders picking fights with company CEOs. By the 1980s, such men were known as "masters of the universe." In many ways, the corporate raiders of the '80s were not so different from the '50s Proxyteers. Both groups featured aggressive and motivated young businessmen operating on the fringes of Wall Street. But while the Proxyteers struck fear into the hearts of CEOs with their ability to harness the discontent of public shareholders, the corporate raiders had something much more powerful at their disposal: ready cash. It came from Michael Milken and the vast market he created for new-issue junk bonds. Milken used his network of high-yield buyers to create a liquidity boom for young takeover artists.

GM's Evolving Ownership Structure

General Motors is a good example of how ownership of America's corporations evolved over time. In 1920, most of GM's shares were held by a handful of "owner-capitalists," as Peter Drucker called them. This group included the DuPont Company and men, like Alfred Sloan, who sold their businesses to Billy Durant in exchange for stock. Over the next 30 years, most of the large individual owners retired from GM's board of directors and passed away. In 1957, the US government forced DuPont to dispose of its large stake in General Motors for antitrust reasons. By the 1960s, General Motors was a modern public company, run by professional managers and governed by a board of directors with little share ownership. From that point forward, institutions would dominate the company's shareholder base.

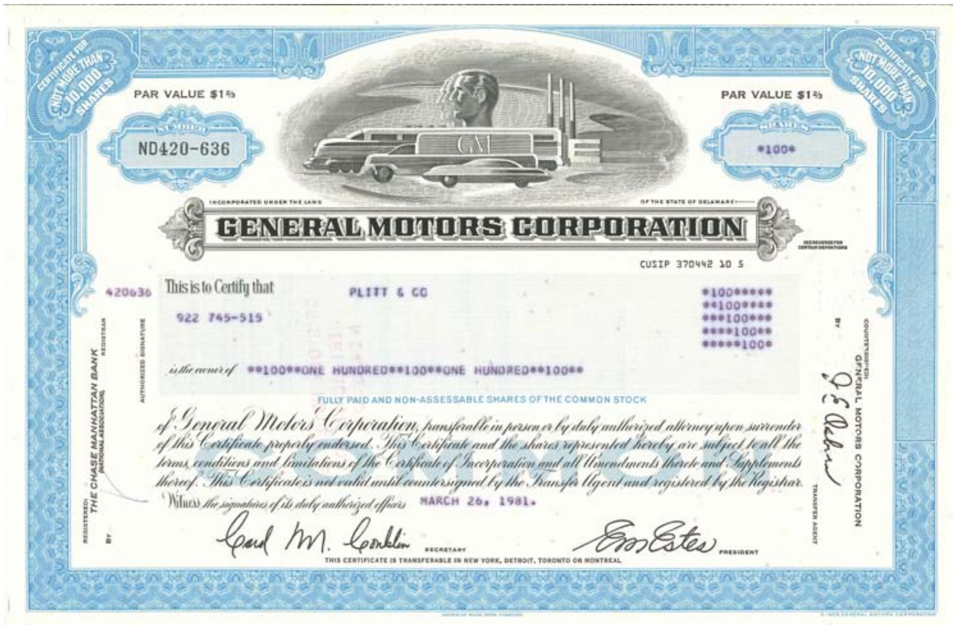
General Motors itself played a major role in this evolution. Employee pension funds, which form one of the largest groups of institutional investors, are essentially a GM creation. While some pension funds existed when GM President Charles Wilson launched the GM Pension Fund in 1950, they tended to be annuity plans holding fixed-income securities, or trusts invested entirely in the stock of the employer company. Wilson believed pension plans should have significant equity exposure, but he thought it was senselessly risky to bet workers' retirement money on the future of their employer. He mandated independent management of GM's pension funds, little or no investment in the employer company and a diversified portfolio with no large ownership stakes in other companies. Wilson's guidelines immediately caught on with other employers — 8,000 new plans were launched within a year of GM's — and were codified in the ERISA Act of 1974.

Corporate America's decision to broadly invest its employees' retirement funds in equities gave American workers a huge ownership stake in the country's economic assets. Drucker argued that this made the United States the world's first truly socialist country. But it also placed control of these investments in the hands of conservative, highly-regulated fiduciaries who limited their exposure to any single investment. Before Ross Perot pushed them to a breaking point, these kinds of investors were highly unlikely to intervene in the oversight of powerful companies like General Motors.

Ross Perot Sparks a Rebellion

On October 23, 1985, Perot penned a scathing five-page letter to Roger Smith, challenging his autocratic management style. He wrote:

> In the interest of GM, you are going to have to stop treating me as a problem and accept me as —
>
> — A large stockholder
>
> — An active board member



Collection of the Museum of American Finance

General Motors stock certificate, dated March 26, 1981. Ross Perot's battle with the company became a turning point in shareholder activism in the United States in the 1980s.

— An experienced businessman

You need to recognize that I am one of the few people who can and will disagree with you…

I do not believe that GM can become world class and cost competitive by throwing technology and money at its problems.

— The Japanese are not beating us with technology or money. They use old equipment, and build better, less expensive cars by better management, both in Japan and with UAW workers in the US.

— We are not closing the quality and price gaps in spite of huge expenditures on automating plants. The fact that we have not set a date to have competitive prices indicates the prevalent attitudes about our will to win.

The foundations for a future relationship are honesty, openness and candor — or simply put, mutual trust and respect. From this point forward, actions count — words do not. We must focus all our energies on helping GM win.

Perot's reason for tackling General Motors was simple: "It was the opportunity to save millions of American jobs. It was too exciting to pass up." This is a man who engaged in many difficult battles over his lifetime and fought to their end. But perhaps none of these was harder than making positive changes at a poorly-run public corporation. Perot's letter turned out to be the breaking point in his relationship with Smith. From that moment forward, Smith focused his energy on getting Perot off the board of directors.

General Motors ended up spending $80 billion on new plants and equipment through the course of Smith's nine-year tenure as chairman, plus another $10 billion for acquisitions of high-tech companies like Hughes Aircraft, whose purchase was approved over Perot's lone dissenting vote. Much of this money was wasted, as was more than $700 million used to buy out Perot in 1986 to make him walk away from GM. One of the world's greatest industrial companies — once a model of good management and governance — was on a path to insolvency.

When the buyout was made public, Perot, who was as astounded as anyone that GM's board of directors would approve such a large payment just to get rid of him, challenged shareholders to do something about it. He said, "I've alerted the stockholders that if they accept this, then they deserve what they get."

Perot's battle with General Motors became a turning point in shareholder activism and public company governance in the United States. Large pension funds that had held GM stock for years without making a peep were aghast that a company would spend $700 million to weaken its board of directors. Institutional investors were finally discovering their voice. Perot ultimately left General Motors without accomplishing any of his lofty goals for the company, but on his way out he stoked a fire under the country's largest institutional shareholders that remains burning today.

The awakening of institutional investors, prompted by the Perot buyout in 1986, had an immediate impact on public company governance. CEOs and directors were targeted in ways that seemed unthinkable just a few years earlier, as evidenced by the California Public Employees' Retirement System's campaign to dump Smith from the GM board. But the biggest effect was at first quite subtle — the stiffening resolve of institutional holders behind the scenes. Shortly after the Perot buyout, the head of the State of Wisconsin Investment Board (SWIB) said, "If shareholders continue to be passive, they will continue to be shorn like sheep."

He meant it. After Perot, you could no longer count on large institutional shareholders to be pushovers. This helped end the corporate raider era, while encouraging the kind of shareholder activism that dominates markets today. $

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Municipal Insolvency in the 1930s

Courtesy of Heritage Auctions

The City of Detroit issued scrip to employees in lieu of paychecks during a cash crisis in 1933, but the effort floundered as local stores refused to accept it.

Cities and States Were in Dire Straits Before They Had Pension Obligations

By Frederick J. Sheehan Jr.

Current worries about municipal solvency focus on pension plan liabilities, with a widely-held belief that if pension problems could be solved, then so too would the troubles of state and city finance. This is a leap of faith. Even if all pension obligations disappeared, financial problems of states, cities and towns would run deep. A review of municipal insolvency in the 1930s — a time when pension obligations were in their infancy — shows how municipal policies designed in good times may turn sour.

The solvency of cities and states looked assured in 1929, at least according to Moody's. That year, the agency rated all of the nation's 25 largest cities Aaa. This was also true for 46 of the 48 states, as well. Yet, in 1932, many of the cities could not sell a bond at any price, and their bonds did not trade. By 1935, at least 3,252 municipalities were in default.

It is an oversimplification to look for a single culprit, but it may be true that if real estate speculation had not run wild, the 1930s would have been different. There is a history of real estate splurges leading to municipal busts. H.C. Adams wrote in 1887: "The mention of the words 'real estate' suggests…a reason why ambitious cities are so willing to incur heavy indebtedness… [T]he bonding of a town, and the expenditure of the money procured in showy works, is the occasion of actual gain to those who speculate in real estate…"

Adams found the "showy works" made the city more attractive, increased property prices and produced more revenue. His observation was held out as a truism in the 1930s. The thousands of showy new schools and athletic facilities being built today offer room for reflection.

A.M. Hillhouse, in his study of municipal bond defaults in the United States, resurrected Adams. In his 1936 book, *Municipal Bonds: A Century of Experience,* Hillhouse assessed "the major portion of overbonding by municipalities arises out of real estate booms." Hillhouse does not dismiss the stock market crash, the production boom, the spending splurge or widespread access to credit by consumers. Rather, he draws his conclusion of the common thread after studying defaults back to 1836. Likewise, there are many other lines of activities that must be addressed to gather a full understanding of what must be corrected today.

Residential real estate topped out in 1925, and commercial building was favored into the early 1930s. The supply of returning soldiers after World War I and the reduction of residential building during the war created a demand for housing. Potential builders were reluctant to fill the void, since construction costs more than doubled after 1914. During that period, apartment rents had not risen. Between 1918 and 1920, residential rents increased by 65% and building costs fell 25%. A nationwide housing boom commenced.

By mid-decade, the balance of building to potential occupants had been restored. Residential real estate then grew speculative and laid waste to municipal budgets by the 1930s.

There was a forerunner. Municipal insolvency already filled the Florida courtrooms by the late-1920s. This might have served as a warning elsewhere. Maybe it looked too fantastic to be believed. In any case, because the Florida land bubble distorted behavior and finance to such a degree, it shows how Adams's claim in 1887 applied in 1932. Parallels to post-millennium excesses are also evident.

Property valuations in Miami rose over 1,000% from 1918 to 1923. Promoters descended on the state. Restaurants and delis in Miami served lines of speculators coffee for 75 cents (with no cream) when the going price for a cup in New York City was a nickel. In the summer of 1925, residents of Miami placed "Not for Sale" signs to ward off the pests. Leases to realtors reached $700 a square foot on Flagler Street in Miami, when similar space at Broadway and 42nd Street in New York — a very desirable location — rented for $13 a square foot.

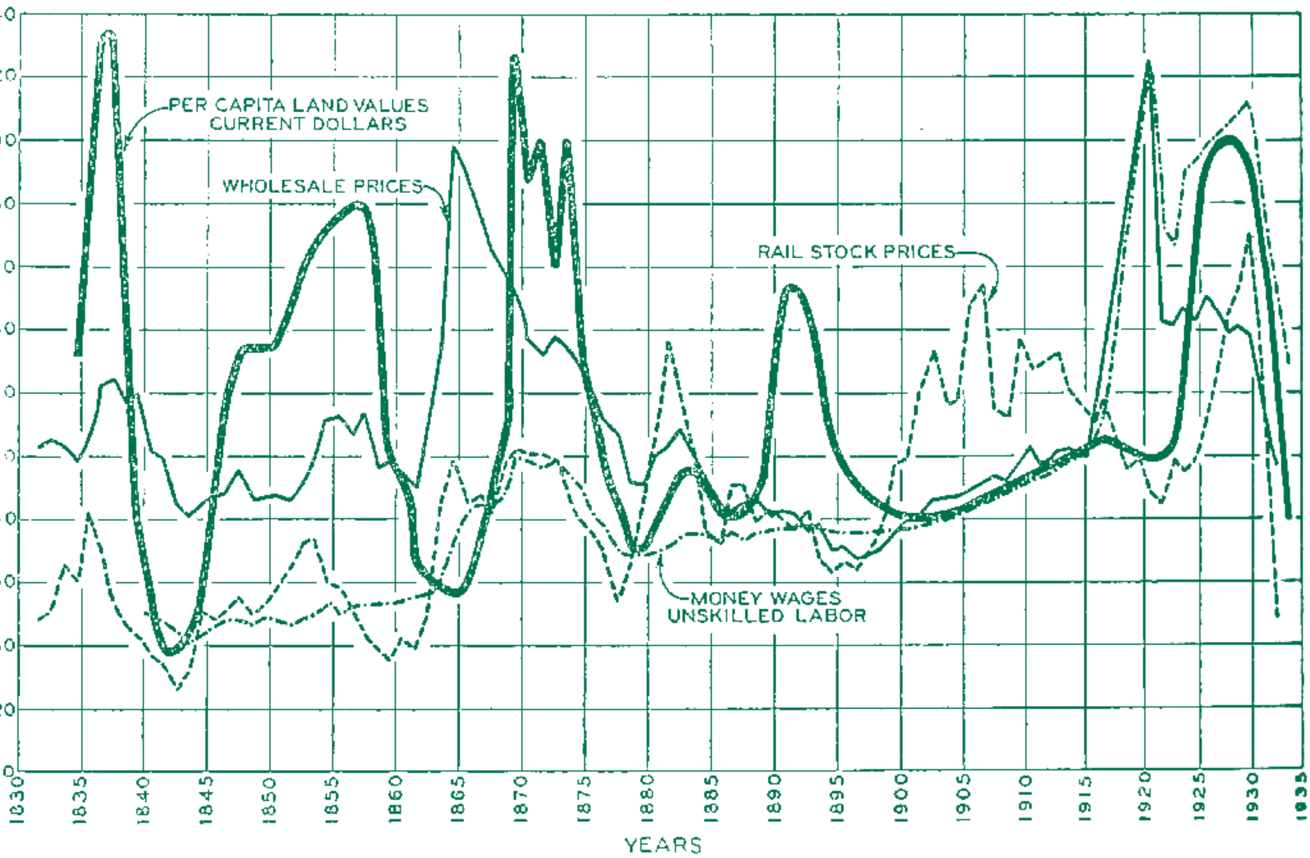
Coral Gables was born in 1921 and posted over $100 million in property sales in 1925. Miami real estate transfers increased in volume from 4,126 in January 1924 to 9,744 in January 1925 to 16,960 in October 1925. Florida was hit with a 125 mile-per-hour hurricane in 1926, and Miami's real estate transfers fell to 4,491 in October 1926.

The realtors and speculators were gone, as was the municipal revenue attached to their fevered activity. Florida was now stuck with high fixed costs that were not easily remedied. (To meet the swirl of activity, Miami's municipal payroll had risen 2,500% between 1921 and 1925.)

Paul S. George wrote in "Brokers, Binders, and Builders: Greater Miami's Boom of the 1920s," that "the amount of individual and corporate financial ruin resulting from its collapse is incalculable." Incalculable, but easy enough to project into the 1930s, when so many tentacles that had boosted municipal revenues — the very sources that had been projected to spend ever more freely and absorb rising public costs — vanished.

George continued, "This speculative era also led many municipalities to institute costly internal improvement programs that were financed by bonds." Coral Gables was saddled with $29 million in creditor claims by 1929.

A common pattern across many cities was for the post-World War I housing deficiency to abate, but for a residue of speculation to weigh heavily on municipal coffers and on the banks holding title to abandoned property. The residential



Chicago per capital land values, compared with wholesale prices, wages of unskilled labor and retail stock prices in the United States, 1831–1933, from Homer Hoyt's *One hundred Years of Land Values in Chicago.*

market peaked in Los Angeles in 1923. By 1924, developers had abandoned 156,557 lots in Los Angeles with an estimated assessed valuation of $1.1 billion and annual carrying costs of $100 million.

In Chicago, residential real estate topped out in 1926, but, given "estimates of future population increase, it [would] take until 1960 to absorb the vacant lots already subdivided in 1928." In Detroit, there was one lot in use for every three lots left vacant. In city after city, "taxes had risen to meet the costs of governing the vast stretches." Tax delinquencies followed.

In 1933, Professor Ernest M. Fisher wrote that the "savings of thousands who had speculated have thus been wiped out. Capital expended in the installation of streets, sidewalks and public utilities lies idle and is rapidly disappearing."

At the 1933 meeting of the American Economic Association, Professor Herbert D. Simpson laid out the dynamic:

> During this period of prosperity, real estate taxes were paid with little complaint… Under these conditions, public expenditures expanded and taxes were increased without protest… The result has been a structure of public expenditure which has been difficult to curtail, and a volume of indebtedness whose solvency is now jeopardized on a large scale.

Simpson continued:

> All the existing resources of existing banking and financial institutions were utilized to the full in financing this speculative movement. The insurance companies bought what were considered the choicer mortgages; conservative banks lent freely on real estate mortgages, and less conservative banks and financial houses loaned on almost everything else that represented real estate in any form… Real estate interests dominated the policies of many banks, and thousands of new banks were organized and chartered for the specific purposes of providing credit facilities for proposed real estate promotions… In the extent to which their deposits and resources were devoted to the exploitation and promotions carried on by controlling or associated interests, these banks commonly stopped short of nothing but the criminal law—and sometimes not short of that.

Nobel Prize-winning economist Robert Shiller calculated that single family home prices dropped 4.1% between 1925 and 1926; 8.2% by 1929; and 12.2% between 1925 and 1930. In 1929, a "period of widespread default" started to accelerate. Over 10% of Chicago real estate bonds were already in default. Assets on the balance sheets of financial institutions were suffering a similar deflation.

Yet the building continued. More generous financing was provided in which the speculator had less to lose. J.E. Morton's description of that period offers similarities to our post-millennial decline in lending standards:

> It is known, at any rate, that there was some tendency in the second half of the '20s for loan-to-value ratios to rise, and for maturities to lengthen, other things may have happened to

lower credit quality, such as more liberal appraisals of property and less rigorous standards in screening loan applications… Among the bank loans made in the years 1920–1929, the frequency of default increased with increases in contract maturity and in loan-to-value ratios.

A current of thought today maintains the cause of the Great Depression was the Federal Reserve's parsimony towards banks in the early 1930s. Yet, it is difficult to understand how such liquidity would have aided those banks that had risen "on a continued advance of real estate values," but "the rate of absorption halted and the price movement stopped, [and] one of the largest categories of bank collateral in the country went stale, and the banks found themselves loaded with frozen assets, which we have been trying ever since to thaw out."

Commercial building grew to a frenzy in the late 1920s. Cities across the country engaged in skyscraper envy. When the president of the National Association of Building Owners and Managers addressed his membership in 1926, he observed that one-eighth of the national income was spent on building:

> Buildings were being put up through the endeavors of bond houses to sell bonds, whether the buildings were needed or not. During 1925, \$675 million of real estate bonds were sold in this country…an increase of more than 1,000% in the last five years. [In fact, later calculations would show that \$54 million were issued in 1921, \$752 million in 1925 and \$833 million in 1928 — the peak, before \$395 million in 1929.] This overproduction is caused by speculative builders, who borrow the full cost of the construction regardless of return. They then sell the buildings at a profit and proceed to erect another somewhere else.

Once in motion, commercial building does not stop on a dime. New York City office space rose 92% in the back half of the 1920s and by another 56% after the stock market crash. Two weeks before the stock market crash, the *New Yorker* described to its readers the feverish levels of speculation and desperation:

> [M]any contractors of estimable standing are ready to take over the 'secondary financing' of not-too-large operations, meaning they will put up most of the cash necessary to complete the building, over and above what the first mortgage provides. They do this in order to keep their operation from falling apart. This loan for the building, which is really a second mortgage, is discounted at some 'big, friendly bank,' so that the contractor's money is not tied up after all…

The *New Republic* critiqued the 1932 skyline:

> [W]inter evenings were cruelly revealing, for when the sun set before the close of daily business it was all too apparent how many of these towers stood black and untenanted against the stars… With some few exceptions, the newest New York may be described as a 60-story city unoccupied above the 20th floor.

That description may serve as a metaphor regarding the state of municipal finance by 1932. Between 1912 and 1932 local government expenses increased 361%, state government spending rose 100% and federal government spending rose 13%. There had probably been little consideration of access to funding (or the ability to raise taxes) during the good times. By the end of 1931, Chicago and South Carolina could not issue notes or bonds at any rate. By December, municipal bond dealers were no longer willing to hold municipal bond inventories. It was nearly impossible to get price quotes for a wide range of municipal bonds. Arkansas and Detroit defaulted. Employees were paid with scrip.

Dominoes continued to fall. Often, the concession required by potential bond buyers was to cut payrolls and salaries. Between 1930 and 1933, every form of municipal expenditure had been cut with the exception of relief payments.

All manner of deplorable practices became clear when cities begged bondholders and banks for loans. Barrie Wigmore, author of *The Crash and its Aftermath*, wrote of 1933:

> The turmoil over municipal credits begat a long list of criticisms of municipal practices that had been acceptable in previous, less contentious times. The practical power of local governments to alter their commitments to bondholders was fundamental and quite startling, but besides that, critics claimed that municipal accounting practices were lax, employed shifting standards, lacked audits, and hid obligations that had accrued.

All of Wigmore's observations ring true today. We know irregular accounting practices are so ingrained they are taken for granted. The *Chicago Tribune* reported on November 1, 2013: "General obligation bonds are intended to help governments achieve lasting public works — such as libraries and bridges — that are too costly to pay for all at once. But records show Chicago's city leaders exploited a loophole in federal tax law and pushed the boundaries of Internal Revenue Service rules that prohibit using this type of borrowing for day-to-day expenses."

We already see cities and claimants battling each other in court. This is during a time that is relatively good compared to the municipal precipice between 2009 and 2011. Detroit today might be seen as an outlier, but it may be a forerunner, such as Florida was in the late 1920s. There is a rising docket across the country of bondholders, banks and elected as well as appointed government figures pointing fingers and fighting over an irreconcilably smaller pot than can satisfy the parties. Pension claims, which have been exempted from this study, are the largest promise of all.

We can be certain of surprises ahead. In 1933, tempers flared when the Iowa Supreme Court ruled the City of Dubuque was required to meet its bond commitments. *The New York Times* headline of the ensuing fracas serves as a warning: "Iowa Farmers Abduct Judge From Court; Beat Him and Put Rope Around His Neck." $

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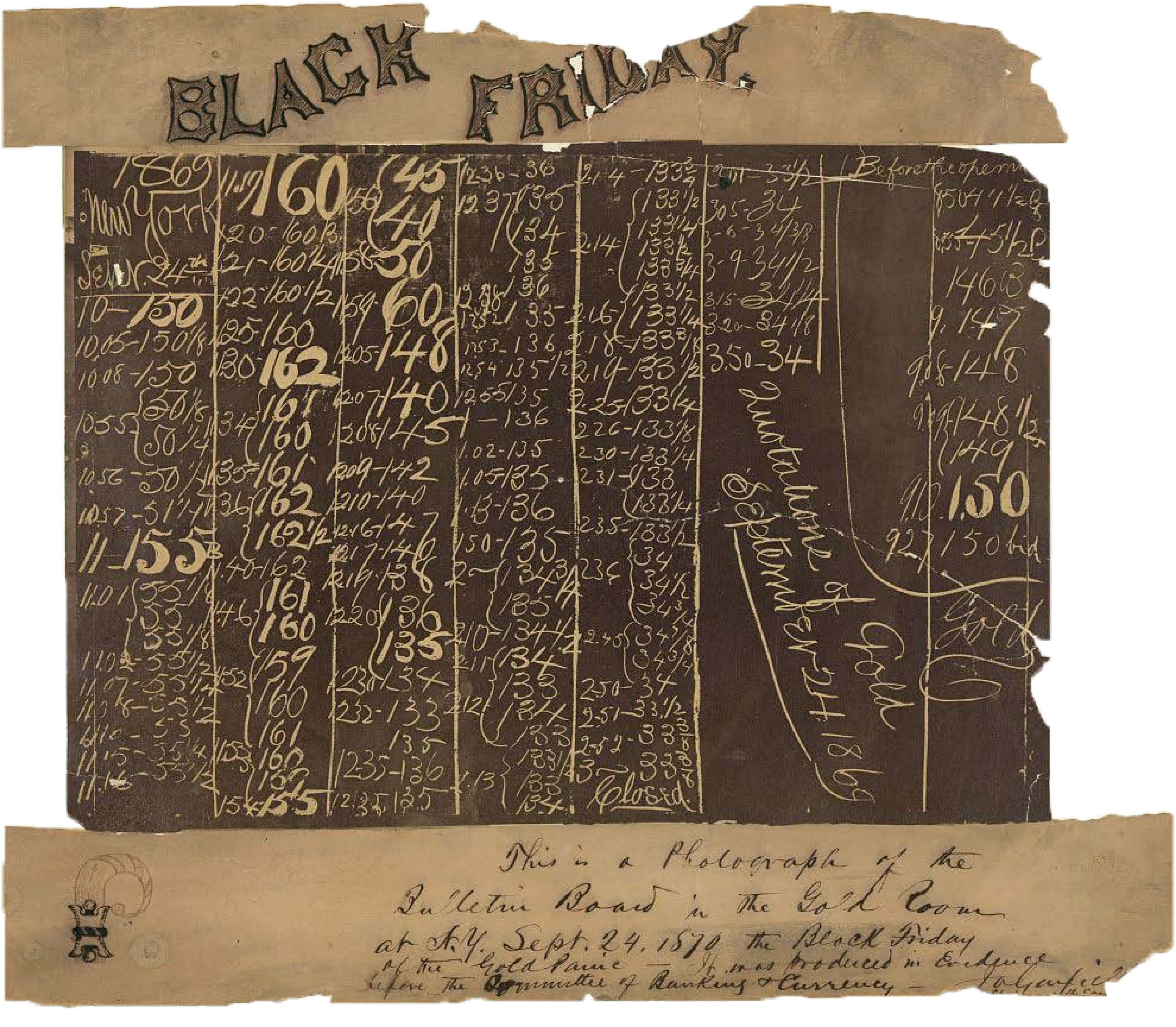
AMERICA'S FIRST

BLACK FRIDAY

The Gold Panic of 1869



Library of Congress

Photograph of the bulletin board in the gold room on Black Friday, September 24, 1869, showing the collapse of the price of gold.

Collection of the Museum of American Finance

Jay Gould

Collection of the Museum of American Finance

Jim Fisk

By Donald P. Morgan and James Narron

Wall Street in the late 1860s was a bare-knuckles affair plagued by robber barons, political patronage and stock manipulation. In perhaps the most scandalous instance of manipulation ever, a cabal led by Jay Gould, a successful but ruthless railroad executive and speculator, and several highly-placed political contacts, conspired to corner the gold market. Although ultimately foiled, they succeeded in bankrupting several venerable brokerage houses and crashing the stock market, causing America's first Black Friday.

A Man, a Plan, a Railroad

Jay Gould was the president of the Erie Railroad. He and "Jubilee" Jim Fisk, his vice president and fellow robber baron, had a plan to corner the gold market and had the political connections to pull it off, or so it seemed. At the time, the Treasury was headed by Secretary George Boutwell, and it sold gold every week in exchange for US Treasury greenbacks — the unbacked (fiat) currency issued by the Union to fund the Civil War. Gould and Fisk schemed to convince President Ulysses S. Grant, who they knew socially via his brother-in-law, to halt those sales and give them room to corner the market.

Through a series of meetings with the President over the summer of 1869, Gould advanced his "crop movement" theory to justify driving gold higher. His theory was that the business interests of the country required an advance in the price of gold; that, in order to move the fall crops and secure the foreign market for US grain, it was necessary that gold should be put up to $145.

Gould was essentially arguing that raising gold prices would devalue greenbacks and, thus, make US crops cheaper abroad and boost exports. That stimulus would, in turn, relieve what he perceived as a "general business dullness" prevailing at the time. Left unsaid was that he and Fisk would benefit on two fronts: first, from the rise in gold prices and, second, from increased crop movements via the Erie Railroad, in which they were major shareholders.

Although President Grant was reportedly tight-lipped during these meetings and refused to reveal his thoughts on the crop movement proposal, he eventually wrote to Secretary Boutwell expressing doubts about continued gold sales. Boutwell responded by pausing them.

Extraordinary Fluctuations in Gold

When Gould and Fisk learned that gold sales had been halted (from an Assistant Treasurer they had bribed for inside information), the two men accelerated their purchases. As gold prices rose quickly over a matter of days, President Grant began to suspect their motives. The President also worried that his brother-in-law, Abel Corbin, was involved. He had the First Lady, Julia Grant, write Corbin's wife, his sister Jennie, informing her that the President was "very much annoyed by your speculations. You must close them as quick as you can."

On the evening of Thursday, September 23, President Grant met with Secretary Boutwell to discuss the precipitous rise in gold prices. He granted Secretary Boutwell permission to break the suspected corner by selling $4 million in gold. That was a considerable amount relative to the overall market of about $15 million.

Foiled!

September 24 started in a frenzy as "bears and bulls jammed the floor…an hour before the opening." Gold opened at $145 but quickly spiked to $160. Fisk planned to continue "bulling" gold, but when Gould caught wind of the pending Treasury sale, he reversed course and began quietly selling without telling Fisk. When news of the Treasury sale finally reached the other traders, "prices galloped like mad; from $160…to $133."

The aftermath was chaotic, and the gold room closed for several days as clerks tried to match sales from heavy trading

Certificate for shares in the Erie Railway Company, signed by Jay Gould as president, October 13, 1869.

throughout the week. The stock market fell 20% as speculators who had shorted gold had to fire-sell other securities to cover their shorts. Several venerable brokerage houses went bankrupt.

To protect himself, Gould paid off William "Boss" Tweed and some New York judges to delay the settlement of unfavorable trades, and he ultimately escaped with his wealth intact. Fisk, who had been buying gold contracts on behalf of other investors, simply reneged on his obligations and also came out unscathed. Neither ever spent a day in jail. Three years later, Fisk was murdered in mid-town Manhattan by a romantic rival who was trying to extort him.

Was Gould's Rationale Plausible?

If you look past all his scheming and conniving, Gould may have actually had a point. US monetary policy in the late 1860s was de jure contractionary; the Contraction Act of 1866 required the Treasury to retire greenbacks with gold with the goal of eventually returning to the gold standard at the pre-Civil war parity. Those 19th century "open market operations" contracted the money supply by 20% between 1865 and 1867, which triggered a severe deflation that fell especially hard on heavily indebted farmers (by increasing the real value of their debt burden).

Against that monetary and macroeconomic background, Gould's proposal made some sense. His perception of a "general business dullness" was on target. According to official recession designations, the economy slipped into recession in June of 1869. Gould was essentially urging President Grant to adopt a more expansionary, or at least neutral monetary policy (by halting greenback purchases), which would lead to currency devaluation and stimulate exports.

Easier money and devaluation are standard prescriptions for a contracting, deflationary economy. While Gould's motives and machinations were suspect, to put it mildly, his diagnosis of an ailing economy and his policy prescription were reasonable. But that's our, possibly unorthodox, opinion. $

Reprinted from Donald P. Morgan and James Narron, "Crisis Chronicles: The Gold Panic of 1869, America's First Black Friday," Federal Reserve Bank of New York Liberty Street Economics *blog, January 15, 2016, available at http://libertystreeteconomics.newyorkfed.org/2016/01/crisis-chronicles-the-gold-panic-of-1869-americas-first-black-friday.html.*

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A Self-Made Man on Wall Street

The Rags to Riches Story of Elias Cornelius Benedict

Courtesy of the Greenwich Historical Society

Photograph of Elias Cornelius Benedict on the south veranda of the palatial manor he built for himself and his family in 1895. It remains there today, still a private residence located at the entrance to Indian Harbor in Greenwich, Connecticut.

By Whitney McKendree Moore

A notable photograph of an accomplished yet little-known financier named Elias Cornelius Benedict shows him on the south veranda of the palatial manor he built for himself and his family in 1895. The home still stands today — a private residence located at the entrance to Indian Harbor in Greenwich, Connecticut. From this home, Benedict commuted to Wall Street — by yacht in fair weather months — magnanimously extending the invitation to anyone who was heading to Wall Street to come aboard, provided they arrived by 7:00 a.m. sharp.

On Wall Street

Wall Street was where Benedict made his fortune. He had ventured there from his home in upstate New York in 1849, a mere 15-year-old boy with nothing but a grade school education. Family legend tells of his early propensity for bargaining, which surfaced early on. The story goes that Benedict, then living in Oneida, New York, overheard a salesman trying to sell a telegraph to a local businessman, who was skeptical about the efficacy of the crazy contraption and was loudly expressing doubts as to its speed.

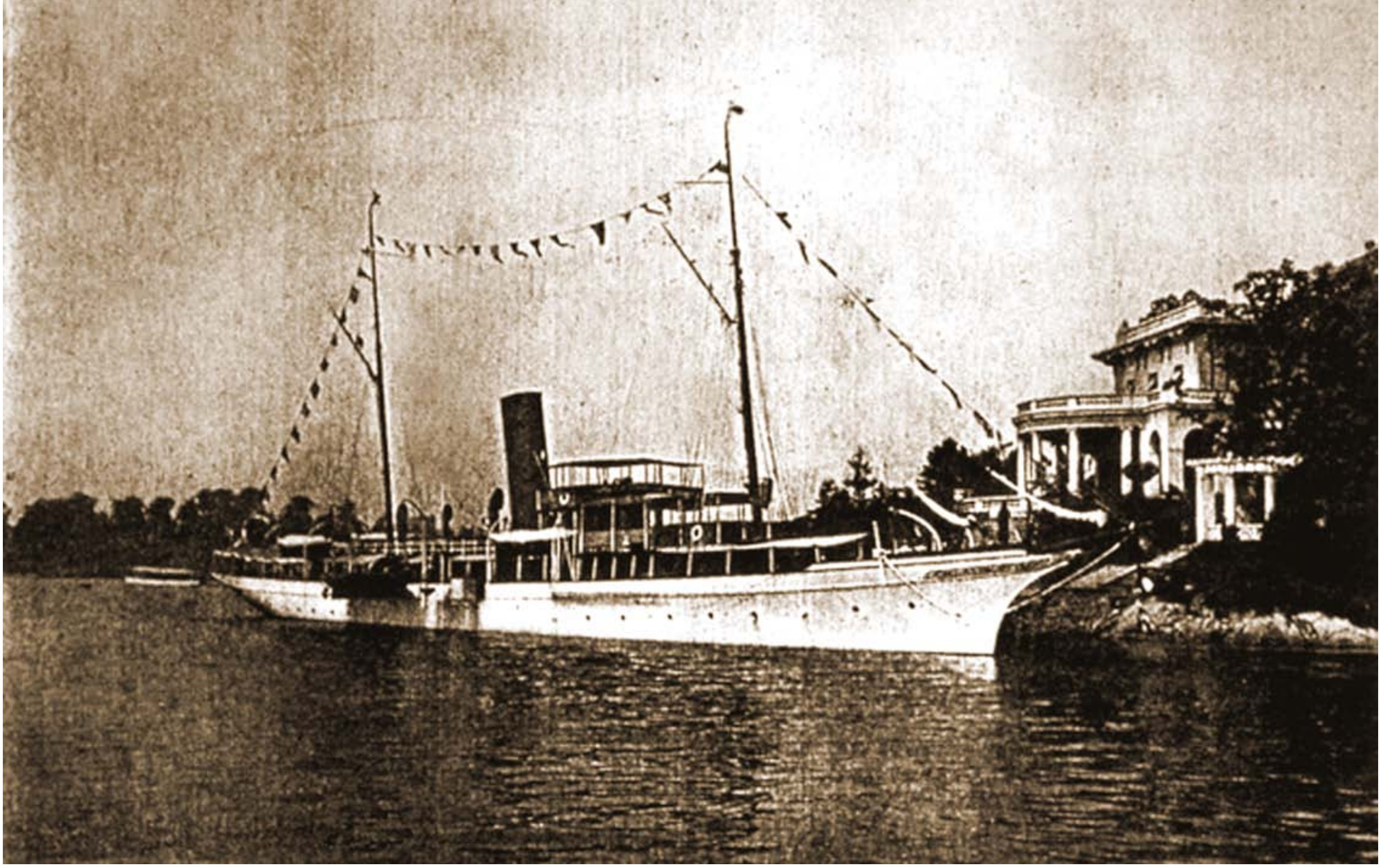
Young Benedict, who then called himself "Corny," could not resist getting into the fray. He wiggled closer to the grown-ups and interjected to suggest an experiment. "Excuse me, sirs, but what if a message could be sent by telegraph to Oneida while I, at the same time, run the same message there on horseback? Wouldn't that prove which one's better?"

The two men stopped their banter to consider Benedict's earnest young face and audacious proposal. Their silence was brief. "Can you find a horse?" one asked the other. The answer was a definite nod. Thus, Benedict, with a good horse, rode as fast as he could toward the town of Oneida. Of course, the telegraph message got there first, and all doubts about the new technology were dispelled.

Not long after, Benedict struck out for Wall Street, joining his older brother, Henry, there in 1849. He started out as a "go-for" at Corning & Corning and must have worked hard to learn the inner workings of Wall Street, as he was able to penetrate the "clique of old men" who ruled over the Financial District at the time. One of the elders, Henry T. Morgan, nominated Benedict for membership in the New York Stock Exchange in 1863. Despite four black balls, he was balloted and elected to his own seat on June 5, 1863 — just in time to reap profits from the Civil War.

This was quite an accomplishment for a young man at the time. Benedict's great grandson, the late Chalmers Benedict Wood of Princeton, New Jersey, said it was unlikely that he ever saw military action, but that he contributed to the war effort nonetheless. "Knowing [Benedict's] ego," Wood said in 1987, "my guess is he did not serve in the Civil War or he would have left countless stories of his heroics. It seems far more likely that his role was to help meet the demands of war on the financial fronts, rather than on the military battle fronts."

Apparently those demands were considerable, as the Union was struggling for money to support its army and turned to Wall Street for needed backing. "A smart investor and capitalist [during the Civil War] could invest in enterprises — clothes, shoes, repeating pistols and rifles — to



Courtesy of the Greenwich Historical Society

The yacht *Oneida* at Indian Harbor in Greenwich, Connecticut.

give the North a crushing advantage over Robert E. Lee and his men," said Wood. "I would guess that my great grandfather, always a leader in technology, probably invested in Colt revolvers made in Connecticut."

Benedict's firm was located at 24 New Street, where his partner from 1871-1875 was Roswell Flower, who later became governor of New York. The business was called Benedict, Flower & Company during this period. Then, in 1876, the Flower portion of the company name was removed, and the firm emerged with a new name (E.C. Benedict and Company), a new location (18 New Street) and a new partner (Benedict's brother, Henry). Henry was president of the Gold Exchange Bank, which he and Corny organized following the gold speculation in 1873.

Benedict earned the bulk of his fortune as a handler of public utilities and gas stocks. He saw considerable success and was eventually reported to be worth $3 million. This may not sound like an enormous fortune today, but in the late 1800s it was amply sufficient to provide for his wife and four children, including as many servants as needed to attend them, and plenty of champagne for entertaining numerous, notable guests.

According to Wood, Benedict had some significant business and investing successes, as well as his share of failures. For instance, he was president of Commercial Acetylene, a gas company, at a time when electricity was yet to be harnessed. It was an era when lamplighters walked the streets every night with their torches to light the gas lamps. Gas was a solid investment — indeed the only game in town — until electricity became commercially available at the turn of the century.

Later, Benedict was heavily involved in backing the invention of the naphtha marine engine using alcohol. All the vapor engines were doomed, however, and the long struggle to devise a practical internal combustion engine for maritime purposes ultimately ceased.

The *Oneida*

Benedict was highly entrepreneurial as a broker, and he took chances on new and untested ideas. Perhaps a primary reason for his financial success was his spirit for adventure. However, it should be noted that his adventurous spirit was not what drew him to yachting later in life. Rather, he pursued this activity on doctor's orders, as he needed a way to offset the stress of Wall Street.

"I took up yachting because I had reached such a state that my physician said I would have to do something of that kind to save my life," Benedict wrote. Characteristically, he took up yachting with exuberance. Other people might have started with a 40-foot ketch or a dignified schooner, but not Benedict. Instead, he acquired a 138-foot steam yacht that carried a crew of 18. He named his yacht *Oneida*, in honor of his former home town and his memorable race against the telegraph.

Aboard his yacht, Benedict not only commuted to Wall Street, but he also led sailing expeditions deep into the Amazon River to explore rubber plantations in regions that were largely uncharted at the time.

The *Oneida* enjoyed much attention from the press, likely for two reasons. Not only was she among the largest steam yachts of the 1890s, but she kept particularly distinguished company. The yacht's log book contained the signatures of such

notables as William Rockefeller, Cornelius Vanderbilt, Andrew Carnegie, Stanford White, Charles Dana Gibson, Ethel Barrymore and Grover Cleveland.

A Presidential Secret

Oneida's biggest claim to fame was in service to President Grover Cleveland who, in late June of 1893, reported a rough spot on the roof of his mouth and was promptly diagnosed as having a malignant cancer of the upper palate. The diagnosis has the potential to be fatal unless an operation was performed immediately.

The US economy at the time was in alarming disarray. The Treasury had been seriously depleted by Cleveland's predecessor, some 500 banks and 15,000 businesses had gone into bankruptcy and Wall Street was in a shambles trying to sort out the effects of these events. Due to the nation's financial instability, Cleveland decided to avoid further panic by having the surgery performed in secret. He asked his friend, Elias Cornelius Benedict, to adapt the *Oneida* (which Cleveland could board, as he often did, without arousing suspicion) by converting its main salon into a makeshift operating room. The physicians and their patient, who arrived by special train, boarded the yacht on July 3, 1893.

It is difficult to imagine any surgery on a President of the United States being kept under wraps. But in July 1893, not one but two surgeries were performed on the President, and both were kept secret for over a quarter of a century — well past President Cleveland's death in 1908.

The Home at Indian Harbor

In 1895, Benedict completed what he must have considered his crowning achievement: an Italianate home on the Greenwich shore known to this day as Indian Harbor. The architect was Thomas Hastings of Carrere and Hastings, who also designed the New York Public Library and the famous Flagler hotels.

Hastings eventually married one of Benedict's daughters, and 2,000 guests were invited to the wedding and reception at Indian Harbor, where they were attended to by 1,700 servants. This kind of opulence was nothing new to the peninsula of land that had previously housed the Americus Club, owned and operated by the notorious William "Boss" Tweed until he was arrested and indicted in the 1870s. According to a local newspaper, Tweed and his followers held their revels there — wine flowing freely, gold being scattered to the winds.

Courtesy of the Greenwich Historical Society

Benedict iceboating on Long Island Sound at age 71 in 1905.

When Benedict acquired the property, the entire edifice was demolished. The dining room, however, was a wholly separate building, ornate to a point surpassing gaudiness. Despite (or perhaps because of) its design, Benedict had it re-purposed as his boathouse. One relative recalled the showplace aspect of the home and Benedict's tendency toward keeping an entourage in tow.

With his massive personality, Benedict had been named "Commodore" of the Seawanhaka Corinthian Yacht Club; and with his fervent interest in exploring all things new, he decided to lead sailing expeditions up the Amazon River in 1905. Instead of risking the *Oneida*, Benedict astutely chartered someone else's yacht to explore how rubber was being farmed. His 1905 expedition aboard the *Virginia* is recorded in *Ten Thousand Miles In a Yacht*, a book published by one of the guests on the three-month voyage. Highlights include descriptions of rubber gathering that somewhat resembled "sugaring off" maple trees in New England. Eventually, the yacht *Oneida* was enlisted to explore the Amazon, stocked with everything imaginable — from snakebite medicine to bandages purchased fresh each spring.

The *Oneida* would then return Benedict to Indian Harbor and a life that was also marked by a high degree of self-sufficiency. Benedict owned a gas company, so there was gas for the entire estate. "It had everything," recalled the late Dr. Horace Bassett, whose father ran the household help. "It had a windmill, so it drew its own irrigation to water flowers and food grown in the gardens."

Wall Street Advice

Looking back on his long life and career, Benedict said, "As I have told young men who have applied to me for advice, don't try to compete with the Standard Oil Company; don't try to compete with the United States Steel Corporation. Turn your attention to places where the colossal corporations and people do business; hold your hat on the other side of the counter at which they spend their money. They will spend their money. Hold your hat where it is going out."

Benedict's lifetime spanned 22 presidents, from Andrew Jackson through Woodrow Wilson, and the advances he witnessed must have boggled the mind. He saw the telegraph invented, gold discovered in California and the telegraph replaced by the telephone. He helped motor cars replace horse-drawn carriages and saw the Civil War foot soldiers replaced by the fighter pilots of World War I. Benedict's original nickname, "Corny," was supplanted when Benedict became known, even on Wall Street, as "The Commodore."

"For 64 years I was in Wall Street, the center of our financial storms in this country and the reflex of all the financial storms abroad, and how I was able to stand it I do not know, unless it was through the inherited strength I possess," Benedict wrote on his 79th birthday. "And speaking of Wall Street, I would like to say that I never invited anybody to go into it, and I have invited many to stay away from it." $

Whitney McKendree Moore grew up sailing in Greenwich, Connecticut, where Commodore Benedict was (and still is) legendary. Among her published works is an article on him that appeared in the Nautical Quarterly (Number 49). *She still writes for publication and is now helping others publish their own books and stories.*

Wall Street Women Celebrate Milestone

The Financial Women's Association Marks 60 Years of Leadership in Advancing Women on Wall Street

President Katrin Dambrot and other leaders of the Financial Women's Association ring the Nasdaq closing bell to mark the organization's 60th anniversary in 2016.

By Kimberly Weinrick and Ria Davis

The financial world is evolving and becoming more diverse—from the Buttonwood Agreement of 1792 when a group of men formed the beginnings of the New York Stock Exchange, to the "Rosie the Riveter" era when women worked at the Exchange while men fought overseas, to the present with many women in C-Suite and other senior leadership roles—there has been tremendous progress in the industry. However, there is still much more to achieve.

Many financial services firms are committed to increasing diversity across their organizations, in particular by fostering more opportunities for women. The Financial Women's Association (FWA), which marks its 60th anniversary in 2016, aims to accelerate the leadership and success of women across the financial community and in all sectors of the industry, by fostering alliances and preparing the current and next generation of professionals. The FWA is a forum for Wall Street women to network and advance their individual careers, and it offers its members leadership opportunities and the chance to mentor and share their experiences and best practices with young women and students.

To fully appreciate what eight enterprising women achieved when they launched the FWA, it is important to remember the historical and cultural context six decades ago. In 1956, the Dow Jones Industrial Average marked a new high, reaching the 500s; Dwight D. Eisenhower was President of the United States; and the first transatlantic telephone cable, from Newfoundland to Scotland, went into operation.

In the midst of this progress, the founders of the FWA, having been denied admission to the Young Men's Investment Association, decided to form the Young Women's Investment Association (now the FWA) as a forum to share their experiences and advance their knowledge and careers.

The founding members were primarily security analysts, which was the first professional role open to women on Wall Street. Soon the organization grew to include female bankers, brokers, traders, management consultants, financial analysts, portfolio managers, economists, lawyers and more. The one surviving founder, Joan Williams Farr, remains fully supportive of the organization.

As Wall Street has evolved and endured through multiple recessions, major changes in the industry and seismic advances in the role and importance of technology, the FWA has evolved as well. Through the decades, the FWA expanded its membership by, among other things, opening membership to men to allow everyone the benefits of sharing best practices and lessons learned.

Early photograph of Joan Williams Farr, a founder of the FWA, who remains actively involved in the organization.

The organization that served as a beacon for the few women on Wall Street in the 1950s continued through the 1960s as a forum for building on shared experiences, while expanding its scope to bring outside speakers to help members hone their craft and advance the profession. The mission broadened even further in the 1970s, as the FWA committed to supporting the next generation through scholarships and mentoring.

> "One striking strength of the FWA was its ability to provide its members with not only some of the resources necessary to learn to maneuver on Wall Street, but also to provide a female space for the women to meet one another and build important ties and friendships with one another."
>
> —*Dr. Melissa S. Fisher, Visiting Assistant Professor in the Department of Social and Cultural Analysis at NYU, and author of* Wall Street Women

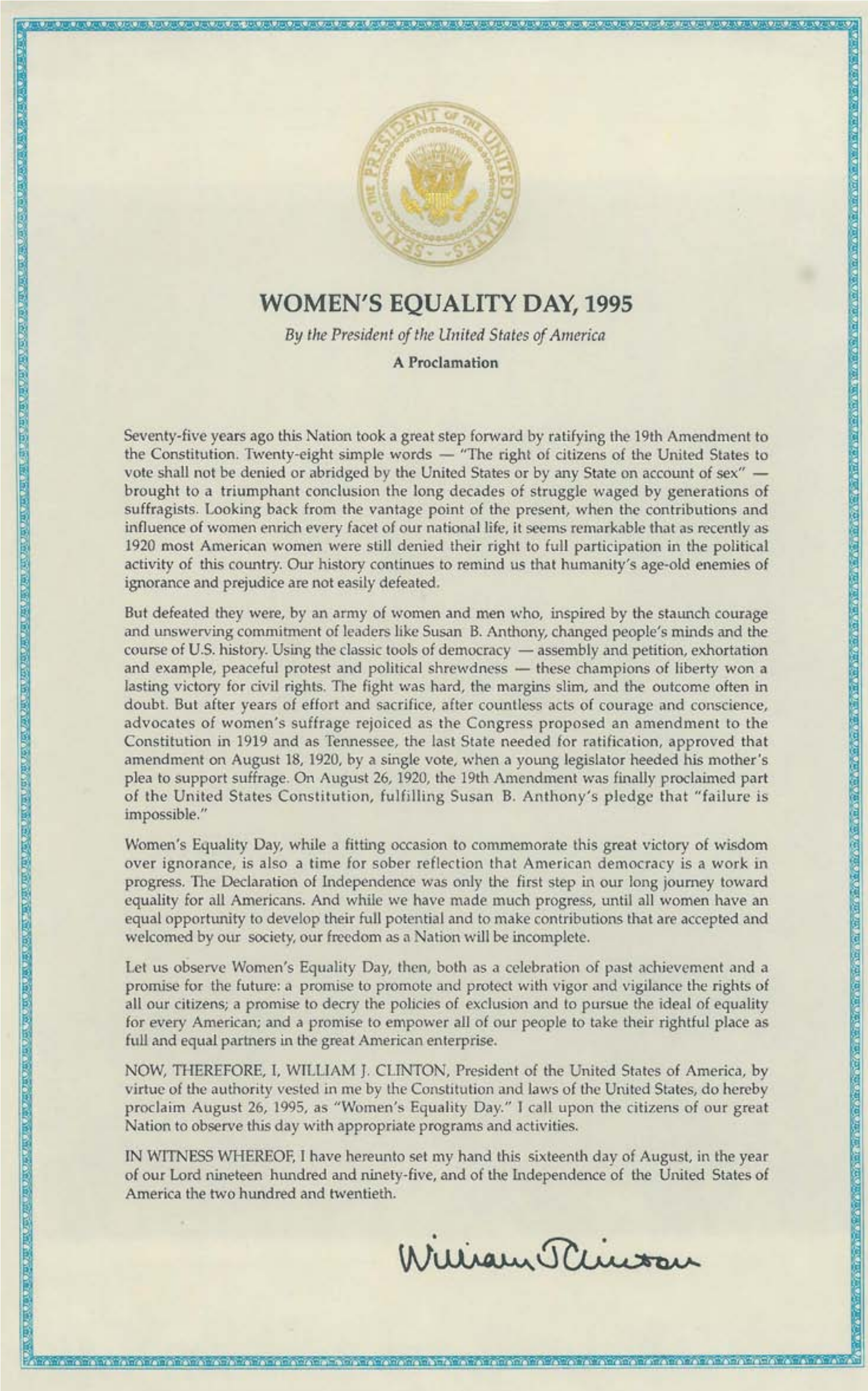
Today, the FWA's initiatives are even more multi-faceted, with more than 50 programs hosted annually. It has awarded more than 150 scholarships and has taught financial skills to nearly 3,000 high school students. It has also provided professional development and mentorship opportunities to thousands of students and young professionals.

Through its outside speaker programs, members and guests have benefited by hearing from and engaging with industry leaders, including Jamie Dimon and Marianne Lake of JPMorgan Chase; Steven Kandarian and Marlene Debel of MetLife; and the late Muriel ("Mickie") Siebert, the first woman NYSE member, who was also an FWA member, supporter and FWA 1994 Private Sector Woman of the Year.

The FWA has also been in the forefront of sending delegations around the world. It was one of the first US groups to visit China in 1977; the delegation of 25 women led the way for an international conference program that continues to this day. Other notable FWA international conferences have included a delegation to South Africa following the fall of apartheid in 1996, Costa Rica in 2010 with new green and microfinancing options and Germany in 2014, 25 years after the fall of the Berlin Wall. Over the years, FWA International Delegation participants have met with sitting presidents, royalty and business leaders in nearly 30 countries and on six continents, some with returning delegations and follow-up meetings and dialogues on best practices.

Of course, none of this happened overnight. In her book *Wall Street Women* (Duke University Press, 2012), Dr. Melissa S. Fisher chronicles the stories of FWA members and other trailblazers, and notes that:

> It has become a common understanding that women in the corporate world, particularly during the seventies, were lone pioneers, token women. There were, in fact, very few professional women in each firm at that time: there



WOMEN'S EQUALITY DAY, 1995

By the President of the United States of America

A Proclamation

Seventy-five years ago this Nation took a great step forward by ratifying the 19th Amendment to the Constitution. Twenty-eight simple words — "The right of citizens of the United States to vote shall not be denied or abridged by the United States or by any State on account of sex" — brought to a triumphant conclusion the long decades of struggle waged by generations of suffragists. Looking back from the vantage point of the present, when the contributions and influence of women enrich every facet of our national life, it seems remarkable that as recently as 1920 most American women were still denied their right to full participation in the political activity of this country. Our history continues to remind us that humanity's age-old enemies of ignorance and prejudice are not easily defeated.

But defeated they were, by an army of women and men who, inspired by the staunch courage and unswerving commitment of leaders like Susan B. Anthony, changed people's minds and the course of U.S. history. Using the classic tools of democracy — assembly and petition, exhortation and example, peaceful protest and political shrewdness — these champions of liberty won a lasting victory for civil rights. The fight was hard, the margins slim, and the outcome often in doubt. But after years of effort and sacrifice, after countless acts of courage and conscience, advocates of women's suffrage rejoiced as the Congress proposed an amendment to the Constitution in 1919 and as Tennessee, the last State needed for ratification, approved that amendment on August 18, 1920, by a single vote, when a young legislator heeded his mother's plea to support suffrage. On August 26, 1920, the 19th Amendment was finally proclaimed part of the United States Constitution, fulfilling Susan B. Anthony's pledge that "failure is impossible."

Women's Equality Day, while a fitting occasion to commemorate this great victory of wisdom over ignorance, is also a time for sober reflection that American democracy is a work in progress. The Declaration of Independence was only the first step in our long journey toward equality for all Americans. And while we have made much progress, until all women have an equal opportunity to develop their full potential and to make contributions that are accepted and welcomed by our society, our freedom as a Nation will be incomplete.

Let us observe Women's Equality Day, then, both as a celebration of past achievement and a promise for the future: a promise to promote and protect with vigor and vigilance the rights of all our citizens; a promise to decry the policies of exclusion and to pursue the ideal of equality for every American; and a promise to empower all of our people to take their rightful place as full and equal partners in the great American enterprise.

NOW, THEREFORE, I, WILLIAM J. CLINTON, President of the United States of America, by virtue of the authority vested in me by the Constitution and laws of the United States, do hereby proclaim August 26, 1995, as "Women's Equality Day." I call upon the citizens of our great Nation to observe this day with appropriate programs and activities.

IN WITNESS WHEREOF, I have hereunto set my hand this sixteenth day of August, in the year of our Lord nineteen hundred and ninety-five, and of the Independence of the United States of America the two hundred and twentieth.

William J. Clinton

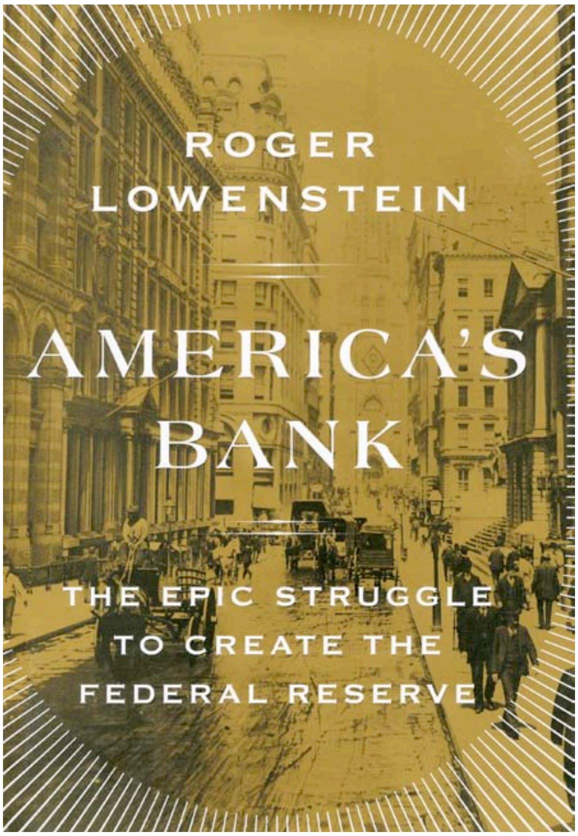
Proclamation signed by President Bill Clinton declaring Women's Equality Day, August 16, 1995.

were only a few hundred on all of Wall Street at the very most. But their isolation actually forced them to seek out other women (like themselves) by attending FWA meetings and in some cases becoming active members of the FWA board. One striking strength of the FWA was its ability to provide its members with not only some of the resources necessary to learn to maneuver on Wall Street, but also to provide a female space for the women to meet one another and build important ties and friendships with one another. This domain was attached to but separate from Wall Street firms. Regularly attending meetings, and forging ties of mutual understanding, they fostered deep friendships that provided emotional support as they dealt with difficult male bosses, for example. This does not mean that the women did not at times compete with one another or even like one another. But to ignore the role of female networks and friendships in the history of Wall Street women's advancement is to obscure the meaning and impact of all female ties on women's careers in finance.

Looking forward, the FWA continues to be a leading partner in professional women's success, dedicated to enhancing the role of women in finance and investing in the community, showcasing outstanding role models and mentoring and inspiring the pipeline of tomorrow's talent. $

Kimberly Weinrick is Head of Public Affairs for OppenheimerFunds, a global asset manager. She is past president of the FWA (2013–2014) and actively serves on its Board of Directors. Ria Davis is General Counsel and Chief Compliance Officer of Semper Capital Management, L.P., an independent investment firm specializing in residential and commercial mortgage-backed securities. She has been a member of the FWA since 2002 and is currently FWA president-elect (2017–2019).

America's Bank: The Epic Struggle to Create The Federal Reserve



By Roger Lowenstein
Penguin Press, 2015
335 pages, $29.95

Even readers familiar with the origins of the America's third central bank will benefit from Roger Lowenstein's *America's Bank: The Epic Struggle to Create The Federal Reserve System.* They will especially appreciate his decision to devote equal time to the financial crises that convinced reformers of the need for some kind of central bank, and the legislative maneuvering that finally led to passage of the Federal Reserve Act.

Lowenstein first tells how financial panics in the late 19th and early 20th centuries prompted would-be reformers to push for changes in the way the nation's fragmented and unorganized banking system allocated credit and managed (or didn't manage) the supply of money. After the election of 1896, a group of academics, bankers and industrialists (operating as the Indianapolis Monetary Commission) proposed a set of reforms that would allow the supply of money and credit to expand and contract to reflect economic conditions. But political and economic leaders in Washington and on Wall Street were not ready to support such reforms, which included an expanded role for the federal government in regulating the financial system. In 1902, Secretary of the Treasury Lyman Gage called explicitly for a government central bank, thus formally and publicly repudiating President Andrew Jackson's famous veto of such an institution in 1835.

Another financial panic in 1907 once again revealed the major fault lines that existed in the nation's banking and monetary system. Senator Nelson Aldrich, Chairman of the Senate Finance Committee, pushed for the establishment of a National Monetary Commission to recommend specific reforms. The author details the nature of that committee's investigative efforts during the following two years. Its final report, published in early 1911, called for the creation of a National Reserve Association of the United States.

Lowenstein then shows how the wrangling over the elements of this Aldrich Plan was only the prelude to the more meaningful debate that emerged as Congress attempted to transform it into a law. The American Bankers Association, the National Citizens' (i.e. Businessmens') League for the Promotion of a Sound Banking System and presidential candidates William Jennings Bryan, Howard Taft, Theodore Roosevelt and Woodrow Wilson all weighed in with suggestions for changes.

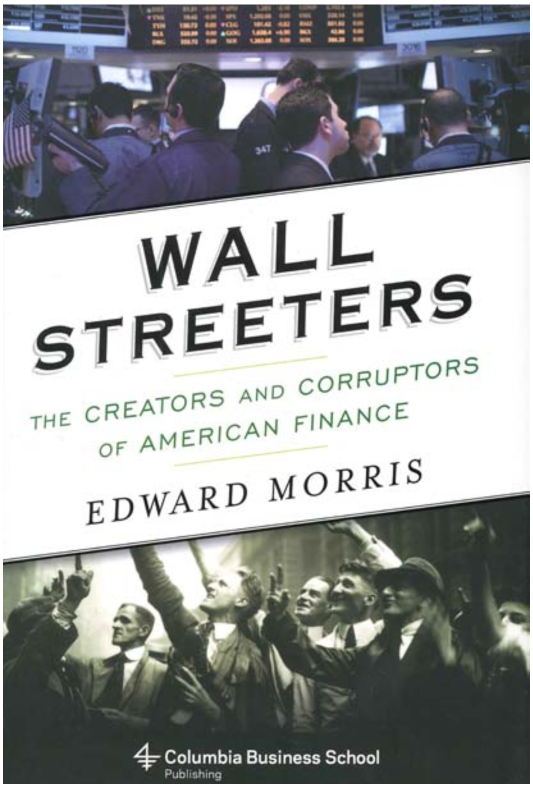
The Democratic Party's consolidation of political power following the elections of 1912 was not accompanied by the emergence of a consensus regarding some key elements of a potential banking reform plan. For example, forces inside and outside of government continued to argue over the ownership and powers of geographically dispersed Reserve Banks, as well as the need for, the makeup and the authority of a "capstone" central bank.

President Wilson tackled other economic problems before turning his full attention to banking reform. By June 1913, he had made his ultimate views on many questions clear enough to permit Congressman Carter Glass and Senator Robert Owen to introduce companion bills that had the President's full support. After a brief period of reconciling still more contentious details, Congress passed and the President signed the Federal Reserve Act in December 1913.

On the book's last page, Lowenstein notes that the creation of the Fed did not guarantee the formation of sound monetary policy any more than the establishment of the US Congress guaranteed the passage of good laws. Moreover, unlike other contemporary authors who have written on this subject, he wisely ends this story of creation without reference to subsequent changes in the powers and actions of the Federal Reserve. $

Michael A. Martorelli, CFA is a Director at Fairmount Partners in West Conshohocken, Pennsylvania, and a frequent contributor to Financial History. *He earned his MA in History from American Military University.*

Wall Streeters: The Creators and Corruptors of American Finance



By Edward Morris
Columbia Business School
Publishing, 2015
329 pages with appendices, $29.95

We are bombarded with market-oriented news and information. Meetings of the Federal Reserve generate as much gossip and speculation as the last royal birth. By any measure, Americans should be the most financially-savvy population in the world. Unfortunately, almost every public and private study confirms that too many people don't know what a rate rise does, what "too big to fail" means or why Wall Street should have less or more regulation. In short, more information hasn't improved the general population's understanding of finance.

This isn't a news flash for readers of this magazine. And we could sit back congratulating ourselves that we think we know more than everyone else. That was largely my attitude when I opened Professor Edward Morris's book, *Wall Streeters: The Creators and Corruptors of American Finance.*

Early on, however, I realized that Morris has produced a book which is a fast and timely primer on how the US got the financial markets it has today. He has cleverly imbedded crucial and complex but sometimes dry financial topics — money supply, central banking, market regulation, securitization and more — within a tour of 14 personalities who created the "Wall Street" America loves and hates. This is a book that every college student, baby boomer and voter ought to read.

Morris goes to central casting for his first profile: the imperious, bulbous-nosed plutocrat, J.P. Morgan. At the turn of the last century, no one matched Morgan's singular ability to control finance through force of influence and personality. This is the starting point for the book, but it is also an ending. There would never be another Morgan because the environment that nurtured him was dying. Financial markets were no longer the purview of a privileged few; they were subject to examination and regulation by progressive elements in America.

Morris next briskly tackles an issue that had been contentious since the country's founding. At the beginning of the 20th century, the United States was alone in the industrialized world in lacking a central bank. Avoiding a long exegesis on the history and theory of central banking, Morris highlights how the home-grown US banking system could not handle the currency and credit flows needed for the rapidly-expanding economy. He focuses on Paul Warburg and Carter Glass, who provided the financial framework and political acumen to get the Federal Reserve in place.

From there, *Wall Streeters* follows the sometimes fast, sometimes slow "democratization" of US finance and financial markets. Charles Merrill, of course, professionalized the brokerage business, broadening and deepening the stock market's reach into Main Street. Where there is wealth, there is greed, and Ferdinand Pecora's unmasking of the corrupt market practices in the 1920s led to the first comprehensive set of financial regulations.

Moving through the mid-century, we meet the men who filled out the array of financial products and offerings that we have today. We learn about the origins of venture capital, hedge funds and indexing, and why they appeal to investors. Morris is entertaining throughout — who knew that socially-challenged Benjamin Graham, father of modern securities analysis, was a serial philanderer?

As the century closes, the complexity of new financial products increases, as does the pace of their introduction. In rapid succession, we meet derivative maven Myron Scholes, junk bond impresario Mike Milken and Louis Ranieri, who saw the value in "securitizing" the most boring of all instruments: the home mortgage. Ranieri's idea, and its toxic off-spring, have recently starred in Hollywood's *The Big Short*.

All in all, *Wall Streeters* is a good read, and a good way to ease non-financial people into how the various moving parts of markets work. I disliked the title — the most cumbersome part of the book – and I wish there was more room for guys like John McChesney Martin (look him up), but these are quibbles.

As the 2016 election heats up, we should do ourselves a favor and read Professor Morris's book so that we may be able to have a sensible discussion about what works and what doesn't work in the US financial markets. $

Jim Prout is a lawyer and business consultant. He can be reached at jpprout@gmail.com.

HOW MUCH DO YOU KNOW ABOUT FINANCIAL HISTORY?

TRIVIA QUIZ

By Bob Shabazian

1. How many income tax returns does the Internal Revenue Service audit each year?

2. Who was Ida M. Tarbell?

3. What territorial acquisition by the United States was labelled Seward's Folly?

4. In the early part of the19th century, what other major land deal involved the United States and France?

5. MetLife is considering the sale of its life insurance units. How did the company get started in the life insurance business?

6. The US Postal Service recently reduced the price of first class postage from 49 to 47 cents an ounce. What was the cost in 1885?

7. The Dow Jones Industrial Average consists of nine sectors. In terms of market capitalization, which is the largest sector?

8. What did the Wilson-Gorman Act of 1894 provide for in regard to taxes?

9. What university has the largest endowment?

10. When did the US Mint become part of the Treasury Department?

1. Nearly 1.4 million, or less than one percent of the 192 million tax returns, according to figures available for 2014. **2.** Managing editor of *McClure's Magazine*, whose investigative journalism led to the eventual breakup of the Standard Oil Trust in 1911. **3.** The purchase of Alaska from Russia in 1867 for $7.2 million. **4.** The Louisiana Purchase in 1803 for $15 million. **5.** It sold policies dealing with Civil War related disabilities. At the end of 1864, the company had written 17 life insurance policies and 56 accident policies. **6.** Three cents an ounce. **7.** Financials **8.** It restored the federal income tax (later ruled unconstitutional but made permanent in 1913 through ratification of the 16th Amendment). **9.** Harvard University, with an endowment of $36.4 billion. **10.** 1873

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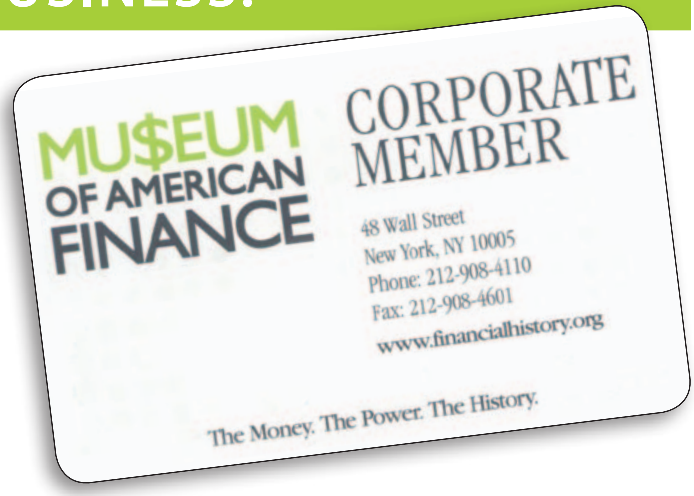

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